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IN THE

Supreme Court of the United States

OCTOBER TERM, 1979

NO. 79-

BRIDGEPORT HYDRAULIC CO.
THE LITCHFIELD WATER CO.

Appellants

v.

THE DIVISION OF PUBLIC UTILITY CONTROL WITHIN THE DEPARTMENT OF BUSINESS REGULATION OF THE STATE OF CONNECTICUT

Appellee

ON APPEAL FROM THE SUPERIOR COURT FOR THE JUDICIAL DISTRICT OF HARTFORD-NEW BRITAIN AT HARTFORD

JURISDICTIONAL STATEMENT

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IN THE

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THE LITCHFIELD WATER CO.

Appellants,

v.

THE DIVISION OF PUBLIC UTILITY CONTROL WITHIN THE DEPARTMENT OF BUSINESS REGULATION OF THE STATE OF CONNECTICUT

Appellee,

ON APPEAL FROM THE SUPERIOR COURT FOR THE JUDICIAL DISTRICT OF HARTFORD-NEW BRITAIN AT HARTFORD

JURISDICTIONAL STATEMENT

Bridgeport Hydraulic Co. and The Litchfield Water Co., the Appellants, appeal from the final judgment of the Superior Court of Connecticut, Judicial District of Hartford-New Britain, dated May 12, 1979, holding that §§ 7, 411.6 and 411.7 of the Connecticut Uniform System of Accounts Prescribed for Class A Water Utilities, on their face and as applied to appellants in rate-making proceedings, do not violate appellants' right not to be deprived of their property without due process of law as guaranteed by the Fourteenth Amendment of the Constitution of the United States.

OPINIONS BELOW

The opinion of the Superior Court, which appears in the appendix hereto, p. 1a *infra*, is unreported.

The decisions of the Public Utilities Control Authority in Docket Nos. 760701 and 770301, which are reprinted at pp. 29a and 47a, are not reported.

JURISDICTION

The opinion and order of the Superior Court were entered May 12, 1979. Appellants sought review in the Connecticut Supreme Court by way of certification and by way of appeal. Appellants' petition for certification was denied by order of the Connecticut Supreme Court dated July 24, 1979. P. 23a. A timely motion for reargument and reconsideration of the petition for certification was denied by order of the Connecticut Supreme Court dated September 19, 1979. P. 24a.

On October 2, 1979, the Connecticut Supreme Court dismissed the appeal which had been taken to that Court. P. 25a.

Appellants filed notice of appeal to this Court with the Clerk of the Superior Court for the Judicial District of Hartford-New Britain at Hartford on November 21, 1979.[1] P. 27a. This appeal is being docketed in this Court within 90 days of the denial of appellants' motion for reargument and reconsideration of their petition for certification by the Connecticut Supreme Court.

The jurisdiction of this Court is invoked under 28 U.S.C. § 1257(2). This Court's opinions in *Sultan Railway & Timber Co. v. Department of Labor & Industries*, 277 U.S. 135 (1928), and *Dahnke-Walker Milling Co. v. Bondurant*, 257 U.S. 282 (1921), sustain jurisdiction over this appeal.

QUESTION PRESENTED

Whether §§ 7, 411.6 and 411.7 of the Connecticut Uniform System of Accounts Prescribed for Class A Water Utilities, which treat the gain on the sale of non-depreciable property that was at one time included in a regulated utility's rate base but is no longer so included as an offset to that utility's operating expenses, thereby *pro tanto* reducing the revenues allowed the utility and passing the benefit of the gain to the utility's ratepayers, are invalid because, on their face and as applied to appellants, they deprive appellants and their investors of their property without due process of law.

[1] In order to assure compliance with the provisions of Rule 10.3 of this Court, notices of appeal were also filed with the Clerks of the Connecticut Supreme Court and of the Superior Court for the Judicial Districts of Fairfield at Bridgeport and of Litchfield on November 23, 1979.

CONSTITUTIONAL PROVISIONS AND REGULATIONS

Sections 7, 411.6 and 411.7 of the Connecticut Uniform System of Accounts Prescribed for Class A Water Utilities are reprinted at p. 90a. The Fourteenth Amendment to the United States Constitution provides ". . . nor shall any State deprive any person of . . . property, without due process of law."

RAISING THE FEDERAL QUESTION

The judgment appealed from was entered in three separate proceedings which had been consolidated for trial. The first of these proceedings was a declaratory judgment action in which appellants were nominal defendants and cross complainants. In their answers and cross complaints, appellants raised their claim that the challenged provisions of the Uniform System of Accounts Prescribed For Class A Water Utilities deny them due process of law by depriving them of their property without just compensation.

The other two actions consolidated for trial below were rate-making proceedings involving the appellants individually. In each proceeding, the challenged accounting regulations were applied to reduce the total revenues to which the appellants were found to be entitled. In their complaints in the appeal from each of these regulatory decisions, appellants challenged the regulatory action as a deprivation of property without just compensation in violation of the United States Constitution.

Appellants' constitutional claims were fully briefed below and were decided adversely by the lower court. Pp. 13a-22a. These claims were presented to the Connecticut Supreme Court, but that court denied review.

STATEMENT OF THE CASE

At all times prior to 1972, the Connecticut Uniform System of Accounts Prescribed For Class A Water Utilities ("Uniform System") provided that gains and losses on the sale of non-depreciable utility property (land and land rights) would be credited or charged to the utility's surplus account. The amount contained in the surplus account constituted a portion of the shareholders' equity and was available for distribution as dividends or for reinvestment. In 1972, however, the Uniform System was amended by the Public Utilities Commission ("Commission")[2] to provide, in §§ 7, 411.6 and 411.7, that gains and losses on the sale of property, including land and land rights, be treated as an offset against utility operating expense if the property sold had ever been part of the utility's rate base. Under the 1972 amendments, the long-term capital gain[3] realized on land which had once been part of appellants' rate base but which is no longer in the rate base because it is no longer used and useful in utility service[4] is credited against appellants' operating expenses. The result is that appellants'

[2] During the pendency of this proceeding, the Connecticut agency charged with regulating public service companies has been denominated the Public Utilities Commission, the Public Utilities Control Authority, and at present, the Division of Public Utility Control. For the sake of simplicity, that body is referred to throughout as the Commission.

[3] Appellant Bridgeport Hydraulic Co. and its subsidiaries, which include appellant The Litchfield Water Co., own 19,924 acres of unimproved real estate. The average cost of this land to the companies was approximately $138 per acre. The parties below stipulated that the present average market value of the land is substantially in excess of $138 per acre.

[4] Connecticut regulatory practice allows a utility to earn a rate of return on its rate base, which consists of the original cost to the utility of its plant, less depreciation and customer advances and contributions, plus an allowance for working capital and materials and supplies. Land and land rights are included in the rate base, at their original cost, only when they are used or useful to the company in performance of its public service obligations. No return may be earned on the cost of land which is not properly includable in the rate base, nor does the utility receive any compensation from its customers for the cost of maintenance, taxes, or other operating expenses associated with land that is not used and useful. Because of changes in technology, including those compelled by the requirements of the Safe Drinking Water Act, 42 U.S.C. § 300f et seq., much of the land held by appellants and once used to provide natural purification is likely in the future to be no longer used and useful in the provision of a safe water supply.

gains on land sales are deemed to yield a *pro tanto* decrease in their utility operating expenses, thereby reducing the amount of revenues appellants are entitled to receive from rates. Cf. *Board of Public Utility Commissioners v. New York Telephone Co.*, 271 U.S. 23, 30 (1926) (order reducing depreciation expense has same effect on net revenues as addition of amount of revenue equal to reduction in expense).

The court below explained the practical result of this change in accounting methods:

> The effect of the amendments which ordered the placement of gains or losses from sale of land in the company income statement (above the line) is that that income may be used by the [Commission] in determining the rates to be paid by the consumer or in reducing that rate. In simple terms, if it were placed below the line (surplus) it is available for stockholders. If it is placed above the line (income) it is available to benefit the ratepayers.[5] Therein lies the struggle — shareholders v. ratepayers.

P. 12a.

[5] The terms "above the line" and "below the line" refer, respectively, to accounts which are included in the calculation of utility operating income and to accounts which are not included in that calculation. The adequacy of utility operating income is the issue in a regulatory ratemaking proceeding. Income that is not utility operating income does not affect the determination of whether a public service corporation is earning a fair rate of return on its properties devoted to utility service. A utility's income statement includes both "above the line" and "below the line" accounts. Appellants do not contest the propriety of accounting for gains on the sale of land in a non-operating income account rather than by crediting such gains directly to earned surplus. Their claim is solely that the Commission's treatment of such gains as utility operating income deprives them of their property.

The effect of the 1972 amendments recognized by the court below is illustrated by the decisions of the Commission in rate proceedings involving both of the appellants. In Docket No. 760701, an application for rate relief by appellant The Litchfield Water Co. ("Litchfield"), the Commission determined that the company had realized a gain on a sale of land in the amount of $108,933.[6] This land had been removed from the company's rate base in 1974 and was sold in 1976.[7] The Commission determined that this gain should be amortized over a seven-year period and as a result included in Account 411.6, for accounting and ratemaking purposes, the amount of $15,562. P. 37a. This action had the effect of increasing Litchfield's net income by that amount. The Commission then concluded that the utility's net income of $25,836 was more than just and reasonable and therefore denied the requested rate relief. Pp. 41a-42a. The amortized gain on Litchfield's land sale represented 60% of the amount found by the Commission to be Litchfield's net income.

In Docket No. 770301, a rate application by appellant Bridgeport Hydaulic Co. ("Bridgeport"), the Commission similarly found that over a five-year period since 1972, Bridgeport had realized an average of $123,000 a year in gain from the sale of land that had once been a part of its rate base. Pp. 77a-78a. After evaluating Bridgeport's application, the Commission concluded that the company's rate of return at its present rates was less than is just and reasonable and that Bridgeport was entitled to a rate of return of 9.5% on its rate base. The Commission further determined that a revenue increase of $1,585,885 would provide Bridgeport with utility operating income sufficient to provide a 9.5% rate of return. P. 86a. If the Commission had not included the amount of $123,000 realized from the sale of land as an offset to operating expenses, the additional revenue necessary to allow Bridgeport to earn the utility operating income deemed appropriate by the Commission would have been increased by $123,000 to $1,708,885. See pp. 86a-87a.

[6] Public service companies can sell land and other assets only with the consent of the Commission. See C.G.S. §§ 16-43, 16-50c.

[7] The 1972 amendments do not distinguish gains that accrued while the utility property was in service, and in the rate base, from those that accrued while the property was not in service, and not in the rate base. The parties stipulated that a number of properties owned by appellants were purchased many years before they were placed in rate base. Additionally, appellants now own a significant amount of land which has been removed from rate base because it is no longer used and useful, and, in the future, will have substantial additional amounts of such land. See p. 9 and n. 10 *infra*. Under the 1972 amendments, gains realized on these properties, which may be held for years by appellants without recompense from the ratepayers, are treated as if they belong to the ratepayers, not to appellants and their investors.

The appeals taken by Litchfield and Bridgeport Hydraulic from the Commission's rate decisions were consolidated with the already pending action seeking a declaratory judgment that the 1972 amendments were invalid. In reaching its judgment that the regulations are valid and that the appeals should therefore be dismissed, the court below recognized that the issue before it was whether the Commission's action constituted "a constitutional [sic] deprivation of property. . . ." P.14a.

To answer this question, the court reviewed decisions from a number of jurisdictions and determined that it would follow the logic and holding of the United States Court of Appeals for the District of Columbia Circuit in the case of *Democratic Central Committee v. Washington Metropolitan Area Transit Commission*, 485 F.2d 786 (1973), *cert. denied*, 415 U.S. 935 (1974). Pp. 14a-17a. The court below adopted the circuit court's conclusion on the central question of whether a regulated utility and its equity investors are entitled, because of their ownership interest, to the profit on the sale of the company's no longer useful property:

> "We cannot accept the thesis that appreciation in value . . . while in operating status automatically flows to [the] investors as inseparable incidents of ownership. *Democratic Central* at 805." [sic]

P. 17a. Following the reasoning of the Court of Appeals, the court then concluded that since the company and its in-

vestors did not have an ownership interest in the gains on land sales, allocation of those gains between the investors and the ratepayers was purely a matter of equitable discretion which should largely be controlled by the validly adopted accounting regulations of the appropriate regulatory body. Accordingly, the court upheld the validity of the 1972 amendments and dismissed Litchfield's and Bridgeport's appeals from the Commission's disposition of their rate applications.

THE QUESTION IS SUBSTANTIAL

I. The Issue Raised Is Important and Has Never Been Decided By This Court.

In *Board of Public Utility Commissioners v. New York Telephone Co., supra*, this Court held that an accumulated excess in a utility's depreciation reserve could not be used by the regulatory authority as an offset to the utility's legitimate depreciation expense in future years. This holding was based on the Court's conclusion that the accumulated reserve was the property of the company. The Fourteenth Amendment prohibits the State from treating the company's property as if it were compensation paid by the ratepayers for utility service:

> Customers pay for service, not for the property used to render it. Their payments are not contributions to depreciation or other operating expenses, or to capital of the Company. By paying bills for service they do not acquire any interest, legal or equitable, in the property used for their convenience or in the funds of the company. Property paid for out of monies received for service belongs to the company, just as does that purchased out of proceeds of its bonds and stock. It is conceded that the exchange rates complained of are not sufficient to yield a just return after paying taxes and operating expenses, including a proper allowance for current depreciation.[8] The property or money of the company represented by the credit balance in the reserve for depreciation cannot be used to make up the deficiency.

271 U.S. at 32.

[8] No similar concession has been made in this case. As explained at p. 11 *infra*, however, the applicable Connecticut statute compels the conclusion that if the gains on land sales were improperly credited against appellants' operating expenses, the rates allowed by the Commission were constitutionally inadequate.

If a regulated utility and its equity owners are the owners of gains realized on the sale of their non-depreciable property, the holding in *New York Telephone* requires reversal of the decision below. Thus, the determinative legal issue in the present appeal is whether the undisputed right of the State to regulate the compensation a utility and its shareholders receive for the provision of utility service justifies the conclusion that the utility and its investors do not have the same ownership interests in property that is no longer being used to provide utility service as do all other corporations and their equity owners.[9] This Court has never addressed that issue.

This issue is of great importance in the State of Connecticut, where many water utilities have large amounts of land which are or will be no longer necessary to the provision of water service. Appellant Bridgeport alone has over 1,000 acres of land which it has removed from rate base because they are no longer used or useful, and on which it therefore no longer receives from its ratepayers either a return on its investment or compensation for the costs of holding the land.[10] The national applicability of the Safe Drinking Water Act, 42 U.S.C. § 300 *et seq.*, suggests that

[9] Connecticut law limits the compensation a public utility may demand for providing utility service, C.G.S. § 16-19 et seq., and requires State approval before property dedicated to public service can be withdrawn from that use, C.G.S. §§ 16-43, 16-50c. It does not otherwise distinguish the ownership interests and rights of a utility and its equity owners from those of any other corporation and its shareholders.

[10] Since 1975, Connecticut water companies have been prevented from selling any land by a "temporary" moratorium on such sales. The original two-year moratorium on sales was extended for two more years in 1977, see *Bridgeport Hydraulic Co. v. Council on Water Company Lands*, 453 F. Supp. 942 (D. Conn. 1977) (3-judge ct.), aff'd., 439 U.S. 999 (1978), and was further extended until June 26, 1980 by the 1979 Legislature. Pub. Act 79-294, 1979 Conn. Legis. Serv. 598 (West).

water utilities in other states are similarly situated.[11] Moreover, the reported decisions demonstrate that allocation of gain on the sale of utility land is a recurring issue in many jurisdictions and with relation to many types of utility companies.[12]

Appellants recognize that regulatory authorities have broad discretion in the areas of ratemaking, *Permian Basin Area Rate Cases*, 390 U.S. 747 (1968); *Federal Power Commission v. Hope Natural Gas Co.*, 320 U.S. 591 (1944), and accounting, *American Telephone & Telegraph Co. v. United States*, 299 U.S. 232 (1936). Connecticut's regulatory scheme, however, removes that discretion from the Commission by establishing a detailed definition of the objectives of rate regulation. The result is that the issue discussed above is clearly presented by this appeal and is decisive of its outcome.

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[11] See n. 4 *supra*.

[12] In addition to the opinion below and to the decision of the District of Columbia Circuit in *Democratic Central Committee, supra,* courts have considered the question of the allocation of gains from the sale of utility land in the cases of *Washington Public Interest Org. v. Public Serv. Comm'n.*, 393 A.2d 71 (D.C. Ct. App. 1978); *Boise Water Corp. v. Idaho Pub. Utils. Comm'n.*, 99 Idaho 158, 578 P.2d 1089 (1978); *City of Lexington v. Lexington Water Co.*, 458 S.W.2d 778 (Ky. 1970); *Chicopee Mfg. Co v. Public Serv. Co.*, 98 N.H. 5, 93 A.2d 820 (1953), overruled on other grounds, *Legislative Util. Consumers' Council v. Granite State Elec. Co.*, 402 A.2d 644 (N.H. 1979); *In Re Revision in Rates Filed by Plainfield-Union Water Co.*, 57 N.J. Super. 158, 154 A.2d 201 (1959); *New York Water Serv. Corp. v. Public Serv. Comm'n.*, 12 A.D.2d 122, 208 N.Y.S 2d 857 (1960); *Keystone Water Co., White Deer Dist. v. Pennsylvania Pub. Util. Comm'n.*, 19 Pa. Commw. Ct. 292, 339 A.2d 873 (1975), aff'd by an equally divided ct., 477 Pa. 594, 385 A.2d 946 (1978). These decisions do not reach consistent results.

Federal regulatory agencies have also dealt with this issue. The Federal Power Commission considers the question to be controlled by *New York Telephone, supra,* and holds that the regulated utilities and their investors receive the benefit of such gains. *Order No. 473*, 49 FPC 390 (1973); *Duke Power Co.*, 48 FPC 1384, 1394-95 (1972). The Federal Communications Commission, on the other hand, considers the question to be controlled by the opinion of the District of Columbia Circuit in *Democratic Central Committee, supra,* and holds that such gains must inure to the benefit of the ratepayers. *American Tel. & Tel. Co.*, 64 FCC 2d 1, 65-66 (1977).

Section 16-19e(a)(4) of the Connecticut General Statutes requires the Commission to establish rates in accordance with the principle

> that the level and structure of rates be sufficient, *but no more than sufficient*, to allow public service companies to cover their operating and capital costs, to attract needed capital and to maintain their financial integrity, and yet provide appropriate protection to the relevant public interests, both existing and foreseeable; . . . .

(Emphasis added.) This statutory language faithfully mirrors the "end results test" on which this Court has come to rely for determining whether a challenged rate order is confiscatory and therefore unconstitutional. *Permian Basin Area Rate Cases*, 390 U.S. at 792; *Federal Power Commission v. Hope Natural Gas Co.*, 320 U.S. at 603-05; *Federal Power Commission v. Natural Gas Pipeline Co.*, 315 U.S. 575, (1942); *Id.* at 607 (Black, J., concurring); *Bluefield Water Works & Improvement Co. v. Public Service Commission*, 262 U.S. 679, 692-93 (1923). In compliance with this statutory mandate, the Commission sets a rate of return and allows revenues which it deems to be "the minimum necessary" to satisfy these functional standards. See pp. 85a-86a.

Since the Commission in its expert judgment has determined that the rate of return established in its decisions is the "minimum necessary," the validity of those orders clearly depends on the propriety of the Commission's treatment of appellants' gains on the sale of their no longer useful land. If those gains belong to appellants and their equity owners, the Commission's orders on their face fail to allow appellants the opportunity to earn revenues sufficient to satisfy the constitutionally required minimum. Accordingly, if this Court agrees with appellants that the Commission's treatment of the gains was impermissible under the Fourteenth Amendment, it should, with appropriate deference to the expert opinion of the Commission regarding the "minimum necessary" rate of return, reverse

the judgment below with regard to appellants' challenges to the Commission's rate decisions. Similarly, if appellants are correct, the Commission's accounting regulations "would clearly and necessarily have the effect of rendering any rate, which is based upon the rule's use, confiscatory in the constitutional sense." *Transcontinental Gas Pipeline Corp. v. Federal Power Commission,* 518 F.2d 459, 465 (D.C. Cir. 1975). Decision of the issue presented by this case is therefore also determinative of the declaratory judgment challenge to the Uniform System of Accounts.

II. The Holding of the Court Below and the Reasoning on Which That Holding Rests Are Erroneous.

The court below did not fully explain why it accepted the conclusion of the District of Columbia Circuit in *Democratic Central Committee, supra,* that gains on the sale of non-depreciable property do not belong to the utility company and its investors. The reasoning of the *Democratic Central Committee* court, however, is fully spelled out in its opinion. 485 F.2d at 800-806. The circuit court reasoned that when this Court rejected the theory that the Constitution requires a present fair market value rate base, see *Smyth v. Ames,* 169 U.S. 466 (1898), in favor of allowing use of a rate base determined from book value less accumulated depreciation, see *Federal Power Commission v. Hope Natural Gas Co., supra,* it necessarily determined that the protected interest of investors does not extend to gains that might be realized on non-depreciable utility property. 485 F.2d at 802. The circuit court also argued that if investors did have a constitutionally protected right in such gains, it would be constitutionally necessary to base a depreciation allowance on the current value of utility property. *Id.* at 803. The Constitution, however, does not require depreciation to be calculated on this basis. *Lindheimer v. Illinois Bell Telephone Co.,* 292 U.S. 151 (1934). Adopting the language of Justice Brandeis, *Missouri Ex. Rel. Southwestern Bell Telephone Co. v.*

Public Service Commission, 262 U.S. 276, 290 (1923) (concurring and dissenting), the *Democratic Central Committee* court therefore concluded that "the central idea [is] that the investor's legally protected interest resides [solely] in the capital he invests in the utility rather than in the items of property which that capital purchases for provision of utility service." 485 F.2d at 801.[13] Accordingly, it held that utilities and their equity owners do not have a constitutionally protected interest in the gains on the sale of utility land.

In effect, the reasoning and holding of the *Democratic Central Committee* case, and the holding below, transform equity investors into bond holders whose sole ownership interest is receipt of a limited return on their investment and return of that investment. This truncation of the equity owner's rights is supported solely by non sequiturs. That a regulated utility and its investors are entitled to be compensated for the provision of utility service by a fair return only on the amount they have invested in property providing that service does not logically entail the conclusion that they are not the owners of that property when it has lawfully been withdrawn from utility service. Similarly, nothing in the principle that depreciation may be based

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[13] Justice Brandeis' full statement does not in any way support the conclusion that a utility and its investors do not own the gain which has accrued on non-depreciable utility property:

> The thing devoted by the investors to the public use is not specific property, tangible and intangible, but capital embarked in the enterprise. Upon the capital so invested the Federal Constitution guarantees the utility the opportunity to earn a fair return. . . . The Constitution does not guarantee to the utility the opportunity to earn a return on the value of all items of property used by the utility, or of any of them. The several items of property constituting the utility, taken singly and free from the public use, may conceivably have an aggregate value greater than if the items are used in combination. *The owner is at liberty, in the absence of controlling statutory provision, to withdraw his property from the public service, and, if he does so, may obtain for it exchange value. . . . But so long as the specific items of property are employed by the utility,* their exchange value is not of legal significance.

262 U.S. at 290 (emphasis added).

on the cost of the capital consumed in providing service, see *Lindheimer v. Illinois Bell Telephone Co.*, 292 U.S. at 168-69, has any bearing on the question of the utility's and its investors' ownership rights in non-depreciable property which has been removed from dedication to the public.[14]

Moreover, were the holding and the underlying reasoning of the court below and of the *Democratic Central Committee* court correct, it would follow that the compensation guaranteed by the Constitution when a private utility is condemned for operation as a public entity would be no more than the utility's book value. Payment of that amount would fully return "the capital . . . invest[ed] in the utility," the only legally protected property interest of the utility or its investors[15] recognized by the holding below and the opinion in *Democratic Central Committee.*

Appellants have found no case which holds that utility property, whether it represents a portion of the utility system or an entire utility, may be taken for public use upon payment of book value. Rather, the cases unanimously agree that the measure of just compensation for such a taking is market or exchange value. The only question

[14] In rejecting the contention that a gas pipeline company's amortization allowance must be based on replacement value rather than prudent investment, this Court explained:

> Even though the reproduction cost of the property during the period may be more than its actual cost, this theoretical accretion to value represents no profit to the owner, since the property dedicated to the business, save for its salvage value, is destined for the scrap-heap when the business ends. The Constitution does not require that the owner who embarks in a wasting-asset business of limited life shall receive at the end more than he has put into it.

Federal Power Comm'n. v. Natural Gas Pipeline Co., 315 U.S. at 593. In contrast, appellants' land is not destined for the scrap-heap, and it has never been treated as a depreciable or wasting asset. The "accretion to value" of appellants' land is not theoretical and, until it was diverted by the actions upheld below, did represent gains to the owners.

[15] The Constitution secures just compensation only for "property" which is taken by public action. E.g., *United States v. Willow River Power Co.*, 324 U.S. 499, 502-03 (1945); c.f. *Flemming v. Nestor*, 363 U.S. 603 (1960) (nature of interests protected by the Fourteenth Amendment).

which has created any difficulty is how that value is to be measured.[16]

In the condemnation context, many cases have noted "the vast distinction between the value for rate-making and the value of property for purchase or condemnation . . . ." *Onondaga County Water Authority v. New York Water Service Corp.*, 285 App. Div. 655, 139 N.Y.S. 2d 755, 763 (1955). In a rate-making proceeding, the question is what is just compensation for the public's *use* of the property devoted by the utility and its investors to public service. In a condemnation proceeding, on the other hand, the question is what is just compensation for the public's *taking* of property which had been privately owned. It is in the condemnation proceeding that it is necessary first to determine the full extent of the private owners' interests.

The condemnation cases establish that the protected ownership interests of the utility and its investors are not limited to "the capital . . . invest[ed] in the utility." The court below, like the District of Columbia Circuit on which it relied, fell into error by taking the measure of compensation for use of utility property as the full measure of the ownership interest of the utility and its investors in non-depreciable property that has lawfully been withdrawn from utility service.[17] By so doing, it allowed the Commission to deprive appellants and their investors of their property without due process of law in violation of the Fourteenth Amendment.

[16] See, e.g., *City of Omaha v. Omaha Water Co.*, 218 U.S. 180 (1910); *Puget Sound Power & Light Co. v. Public Util. Dist. No. 1*, 123 F.2d 286 (9th Cir.), cert. denied, 315 U.S. 814 (1941); *City of Yuma v. Arizona Water Co.*, 22 Ariz. App. 4, 522 P.2d 765 (1974); *South Bay Irrigation Dist. v. California-American Water Co.*, 61 Cal. App. 3d 944, 133 Cal. Rptr. 166 (1976), cert. dismissed, 434 U.S. 801 (1977); *Kennebec Water Dist. v. City of Waterville*, 97 Me. 185, 54 A. 6 (1902); *Onondaga County Water Auth. v. New York Water Serv. Corp.*, 285 App. Div. 655, 139 N.Y.S.2d 755 (1955); *Lake Superior Dist. Power Co. v. Public Serv. Comm'n.*, 244 Wis. 543, 13 N.W.2d 89 (1944).

[17] *Cf. Kaiser Aetna v. United States*, No. 78-738, slip op. at 5-8 (U.S., Dec. 4, 1979) (error to conclude that "navigability" for purposes of congressional regulation subjects property to navigational servitude).

CONCLUSION

For the reasons stated above, this appeal presents an important issue that has not been decided by this Court and that there is substantial reason to believe has been incorrectly decided by the court below. This Court should note probable jurisdiction over this appeal and place it on the calendar for plenary consideration.

Respectfully submitted,

Appellants
BRIDGEPORT HYDRAULIC COMPANY
THE LITCHFIELD WATER COMPANY

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No. 108038

GREENWICH WATER CO., Et Al. vs. HOWARD E. HAUSMAN, Et Al. — SUPERIOR COURT, JUDICIAL DISTRICT HARTFORD-NEW BRITAIN AT HARTFORD, MAY 12, 1979

No. 117874

BRIDGEPORT HYDRAULIC CO. vs. PUBLIC UTILITIES CONTROL AUTHORITY, Et Al. — SUPERIOR COURT at BRIDGEPORT, MAY 12, 1979

No. 015775

THE LITCHFIELD WATER CO. vs. PUBLIC UTILITIES CONTROL AUTHORITY — SUPERIOR COURT at LITCHFIELD, MAY 12, 1979

MEMORANDUM OF DECISION

These cases represent an issue of first impression in this state. The three actions were consolidated by the parties and the courts because they required an answer to what is essentially the same legal question. The Greenwich Water Company (Greenwich) case is an action for a declaratory judgment. The Bridgeport Hydraulic Company (Bridgeport) and Litchfield Water Company (Litchfield) cases are appeals from the doings of the Public Utilities Control Authority (PUCA). Greenwich questions the legality of certain accounting regulations hereinafter stated which were adopted effective January 1, 1972, by the P.U.C.A. *Bridgeport* and *Litchfield* also question the legality of the regulations and, in addition thereto, question the sufficiency of the required notice given by the PUCA antecedent to the adoption of the regulation.

The Greenwich action was initiated in December 1972

and was thereafter stayed because of the pendency of an action before a three-judge federal court brought by *Bridgeport* (*Bridgeport Hydraulic Company, et al. v. Council of Water Company Lands of the State of Connecticut,* U.S.D.C. (Conn.) Civil No. B-75-212,) in which it was perceived by all parties that the federal decision might answer the question of alleged constitutional infirmities which are the crux of the cases here. The federal matter was finally decided with opinion in December 1977. *Bridgeport Hydraulic Company v. Council on Water Co. Lands,* 453 F.Supp. 942, summarily affirmed without opinion, 438 U.S. ——, 98 S.Ct. 2426 (1978).

While the results in the federal action did not resolve the immediate issue here, it did touch on some of those issues and the decision becomes important in noting what it did say and the rationale used in acknowledging the wide power of the state in taking action in controlling the use of privately owned land. Votes in the United States Supreme Court to affirm summarily are votes on the merits of the case. *Hicks v. Miranda,* 422 U.S. 332, 334. *Ohio ex rel Eaton v. Price,* 360 U.S. 246, 247. The precedential effect of a summary affirmance extends no further however than the precise issues presented and necessarily decided by the court below. *Mandel v. Bradley,* 432 U.S. 173; *Illinois State Board of Election v. Socialist Workers Party,* —— U.S. ——, 99 S.Ct. 983, 985 (1979).

Greenwich (the action for declaratory judgment) was presented on a stipulation of fact and was joined in by counsel for *Bridgeport* and *Litchfield.* The stipulation can only apply to Greenwich, inasmuch as *Bridgeport* and *Litchfield* are administrative appeals and the administrative body, PUCA, made its own findings of fact.

Notwithstanding the numerous allegations as to what the issues are, they are reduced to these:

I

Was the required statutory notice given by the old Public Utility Commission in 1971 prior to the adoption of new

accounting regulations, sufficient to put plaintiffs on notice as to the intent of the hearing of the PUC as gleaned from what regulations were actually adopted (Greenwich does not participate in this claim and concedes the notice is proper.).

II

Was the adoption of the new accounting regulations which had the effect of making gains from sales of unused land owned by the company and not then included in the rate base, available for consideration for consumer rate reduction, constitutional and within the power of PUCA to do; and was their adoption an abuse of discretion which prevented the company from earning a fair return on its investment and impaired its ability to attract capital.

WAS THE NOTICE SUFFICIENT

The Public Utilities Commission published notice in the Connecticut Law Journal (July 27, 1971 issue), the following of which is germane here:

"The following is a summary of the proposed changes

1. The adoption of the inclusive income statement in harmony with Bulletin 9 of the AICPA (American Institute of Certified Public Accountants). All items of revenue and expenses, including many previously charged or credited to surplus, with few exceptions will be included in the current income statement.
2. The inclusion of the gains or losses on sale of property held for future use and non-utility property in the other income or other income deductions section of the income statement, as appropriate.
3. Include the gains or losses on sale or other disposition of utility plant, in the utility operating income section of the income statement.

At that time, the process of adoption of regulations was controlled by Sections 4-42 and 4-43 of the General Statutes.

The court notes that the issue of inadequacy of notice was raised for the first time in the combined brief of Bridgeport and Litchfield and thereafter in oral argument. Nowhere is it mentioned in the appeal petition of either. Since counsel placed inordinate emphasis on it in argument, the court will address the issue; after noting that the issue was considered in the federal matter where the notice was found to be proper. *Bridgeport Hydraulic*, supra, 453 F.Supp. at 954, note 6 (3).

In our jurisprudence it is fundamental that a person has the right to notice and he should be given an opportunity to be heard at a meaningful time in a meaningful manner. *Armstrong v. Manza*, 380 U.S. 545, 552, before he can be deprived of any significant property interest. *Boddie v. Connecticut*, 401 U.S. 371, 379. In *Slagle v. Zoning Board of Appeals*, 144 Conn. 690, the Connecticut Supreme Court said at 693:

> "The fundamental reason for the requirement of notice is to advise all affected parties of their opportunity to be heard and to be apprised of the relief sought."

There is no requirement that the notice be an accurate forecast of the exact action which will be taken on the subject matter of the notice. "It is implicit in such a procedure that changes in the original proposal may ensue as a result of the views expressed at the hearing." *Neuger v. Zoning Board*, 145 Conn. 625, 630.

Bridgeport and Litchfield complain that the notice of the hearing gave no indication that the monies received from sales of excess lands would be removed from the surplus account (below the line) where it was available for dividends to stockholders, expansion of plant and other stockholder use, and placed in the utility operating income action (above the line) and available to be used by the PUC in the rate-making process whereby rates charged consumer could be affected and possibly reduced.

A reading of paragraphs 1, 2 and 3 of the notice clearly indicates that the action taken by the PUC was fully within the perimeters therein outlined. As the court in *Neuger*

stated, there is no requirement that the final action taken specifically be a part of the notice. In the notice here, it comes very close to being specific. The conclusion of the court is that the notice was adequate, and fairly apprised those who might be affected by the change so they could make adequate preparation to protest if they so chose, and to offer alternatives.

THE PARTIES

All involved water companies are classified Class A water companies, having annual operating revenue in excess of $50,000.00.

Greenwich is, as are all other water companies involved herein, a private Connecticut corporation located in Greenwich, Connecticut. The amount of land which it owns does not appear. However, all of the privately owned water companies in the state own substantial acres of land in the state.

Bridgeport is a wholly owned subsidiary of The Hydraulic Company. Bridgeport, in turn, wholly owns Litchfield Water Company, North Canaan Water Company, Lakeville Water Company, Cornwall Water Company and the Norfolk Water Company. It owns almost 20,000 acres of land.

The New Haven Water Company is a party plaintiff in the Greenwich Water Company action and owns almost 25,000 acres of land. There are several other plaintiff water companies.

Litchfield, though wholly owned by Bridgeport, brought its own action of appeal and is not a participant in Bridgeport's action for a declaratory judgment.

All the companies are private but operating as public service companies under the regulatory authority of the PUCA pursuant to title 16 of the Connecticut General Statutes. All have shareholders.

The Public Utilities Control Authority (PUCA) is a state agency authorized by law to make regulations respecting class A water companies.

BACKGROUND

Because of increased efficiency and scientific advances in the (1) treatment and purification of water, (2) development of public sewer systems, and (3) the adoption and enforcement of health and environmental laws, there has occurred, from time to time, less need for the watershed land which had been extensively acquired over long periods of time by the utility company. Some of these lands are not needed anymore in the water collection and purification process, have been taken out of the rate base, and are not part of the utility plant equipment any longer. These lands could now be sold at substantial gains over the original cost which averaged about $130.00 per acre.

Thirty-six private water companies own approximately 61,458 acres of realty in the state. Eighty to ninety per cent of this is watershed land which contributes to public water supply reservoirs. The largest owner is New Haven Water Company with 25,000 acres. The smallest is Cornwall Water Company with 8 acres.

Bridgeport and its subsidiaries own approximately 20,000 acres. All of the land except 930 acres were acquired prior to 1948, some acquisitions occurring prior to 1878. The average cost paid for the land over years was $138.00 per acre.

New Haven Water Company with its 25,000 acres, presents a similar picture, with acquisitions going back to 1860. The average paid through the years was $128.00 per acre.

Both Bridgeport and New Haven Water have power of eminent domain. New Haven Water never used it to acquire land and Bridgeport used it to acquire 4% of its purchases. The vast majority of the land was put in the rate base when purchased or soon thereafter and consumer rates were made with that as part of the consideration for rate setting for use of the company's property.

By being a part of the rate base, the consumers, over the years had to pay the utility companies for the use of

the land in providing pure and adequate water, as it was part of the utility plant, although non-depreciable. In the case of Bridgeport, it started to remove the now surplus land from its rate base only in 1972. While it was in the rate base, it was there always as its original cost and not its appreciated value. All the water companies have followed that same general pattern.

Connecticut General Statutes § 16-6b and its predecessors gave the PUCA and its predecessor, PUC, the authority to adopt such regulations with respect to rates and changes, and *accounting practices* as it deems reasonable and necessary. In response to that authority and evident necessity, the commission adopted the Uniform System of Accounts; the first being adopted effective in 1922. There have been made several changes in the system since then by alteration in the system format. Changes were made thereafter in 1942, 1964 and finally in 1972 — which was the catalyst for the present action.

The Uniform System of Accounts adopted by the Public Utilities Commission in 1964 provided that gains or losses on the sale of land be credited or debited to the surplus account (below the line). The surplus account is a portion of the equity of the company and is available for dividends to stockholders or to be invested in additional utility plant. Under the 1964 accounting procedures, this revenue was not available for the reduction of rates or other consumer purposes.

The Public Utilities Commission, effective January 1, 1972, adopted some amendments to the accounting procedures. The pertinent changes had the effect of putting the gains or losses from the sale of excess land that had any time heretofore been in the rate base, into the operation income account (above the line) where it could be used in the rate setting procedures and available to possibly benefit consumers if it were a gain and burden them if it were a loss. Although the PUC adopted the regulations, they never put it into effect by considering the proceeds from the sale of land in the rate-making process and consumers

did not garner any benefits. It was used for reporting purposes only.

The legislature effectively abolished the three-man Public Utilities Commission and set up in its stead in December 1975 the present five-man Public Utilities Control Authority (PUCA). In due time, the PUCA began implementing the accounting procedure changes adopted by the PUC, and began considering gains from the sale of land in the rate-making process. An example is shown in the decision of the PUCA in the application of Litchfield for an increase in rates.

Litchfield sold certain lands which had been previously in the rate base but had been removed from the utility operation as unneeded. There was a net profit of $108,933 realized on the sale. PUCA invoked the 1972 amendments, credited the gain to an operating income gain, and deemed "it appropriate to amortize the net profit . . . over a 7 year period." The gain was amortized into the rate-making structure at the rate of $15,562 per year; the pro tanto effect of which was to reduce the price of water to the consumer and to likewise reduce the amount available to the shareholders as dividends or for plant expansion.

Water companies are assessed for tax purposes the same as the general public or industry generally for similar property. These taxes on the real property are paid by the ratepayers. So are payments for improvement thereon. The property is carried on the book of the company, when in the rate base, at the original purchase price, and the consumer has to pay, in his rates, for the use of that land in helping furnish him water. And even though land purchased in 1860 for $38.00 per acre may have increased in value more than 10,000 per cent over the years, it is still carried on the books at the original cost. Patently, with exploding populations, some of this land has become extremely valuable.

As aforestated, Bridgeport is a wholly owned subsidiary of the Hydraulic Company. The Hydraulic Company has formed another wholly owned subsidiary, Main Street

South Corporation. Main Street South was formed to (1) engage in the real estate business by building, leasing, etc. and (2) acquire real estate from Bridgeport and its subsidiaries at market value and to hold it for present and future development and sale. Bridgeport, in its sale of land, ran afoul of the new accounting procedures and is appealing the doings of the PUCA in this respect.

Bridgeport had sold land from 1972 through 1976, but as aforestated the predecessor Public Utilities Commission had used the amended Uniform System of Accounts since its adoption in 1972, for reporting purposes only and not for a reduction in consumer rates. When Bridgeport came up for its rate increase, the new PUCA not only included gains from sale of land in 1976 but went back to 1972 and applied an average annual gain of $123,000 to reduce the level of ratepaying. PUCA insisted on conformity with the existing accounting regulations.

In Bridgeport's case, some of its lands were acquired through the exercise of its right of eminent domain. New Haven Water Company never acquired any of its land through the exercise of its power of eminent domain. New Haven Water Company has concluded that 15,903 acres of its land, out of a total of 24,733 acres, need not be owned by it in order to carry out its obligations to the public under the statutes, and these lands could be considered for disposal.

THE PUBLIC UTILITY AND PUCA

The concept of public utilities in the United States had its genesis in the acceptance by courts that transportation companies and bailees for hire were "regulatable in England from time immemorial." *Munn v. Illinois,* 94 U.S. 115 (1876). There was thereafter an expansion of the public utility status from the common carrier to other businesses which

> "[H]ave a direct relation to the business or facilities of transportation or distribution — transportation by carriers of passengers, goods, or intelligence by vehi-

> cle or wire; to distribution of water, gas or electricity through ditch, pipe or wire, to wharfage, storage or accommodation of property before the journey begins, when it ends, or along the way." *German Alliance Insurance Co. v. Luvis*, 233 U.S. 389 (1913).

And the government has steadily expanded its regulation of industries which serve the general public and are thereby affected with a public interest. These regulated industries tend toward monopoly, are generally non-competitive, and they tend to operate more efficiently as monopolies. But as such, it is an economic power that is not controlled by the market place and the rates and services have been subjected to governmental control.

As one observes public utilities, he sees that private ownership overwhelmingly dominates. The result is that frequent conflicts occur between the private ownership and public control. The basic objective of the private corporation is the maximization of profits, while the public interest demands adequate service at the lowest possible price. The distances between these two objectives are often large and results in a sort of continuous conflict. The regulated company favors minimum regulation and the public usually demand maximum.

To supervise and regulate the various utilities, the state has created an administrative agency which has vested in it wide powers. This agency was the Public Utilities Commission, now the Public Utilities Control Authority.

Administrative agencies are those agencies of government which usually perform a combined legislative, judicial and executive function. The judicial function is performed through adjudication. The executive function is performed by administering legislative policy, and the legislative function is performed by rule making.

In making rules and regulations which are to govern the activities of a public utility, the state is acting in the exercise of its police power. *Cedar Island Improvement Association v. Clinton Electric Light and Power Co.*, 142 Conn. 359, 370 — That is the power of state to regulate business

to safeguard the health, safety, morals and general welfare of its citizens. The "police power" is not mentioned in the Constitution but has long been recognized by the courts. See *Brown v. Maryland*, 12 Wheaton 419 (1827). *Charles River Bridge v. Warren Bridge*, 11 Peters 420 (1837).

The power to regulate businesses affected with a public interest is not unlimited, however.

> "The Fifth Amendment, in the field of federal activity, and the Fourteenth, as respects state action, do not prohibit governmental regulation for the public welfare. They merely condition the exertion of the admitted power, by securing that the end shall be accomplished by methods consistent with due process. And the demands of due process . . . demands only that the law shall not be unreasonable, arbitrary or capricious and that the means selected shall have a real and substantial relation to the object sought to be attained." *Nebbia v. New York*, 291 U.S. 502, 505.

The method used and the extent of the exercise of the police power is determined by the legislature. *New Haven v. New Haven Water Co.*, 132 Conn. 496, 511. It is unconstitutional if it is exercised in an arbitrary or discriminatory manner. *Cedar Island* at 370.

A legislature may delegate to an administrative agency the power to make rules and regulations for the implementation of a statute, *Kellems v. Brown*, 163 Conn. 478, 499; *State v. Stoddard*, 126 Conn. 623, 628, but the statute to be implemented, to survive constitutional attack must declare a legislative policy, establish primary standards or lay down an intelligible principle to which the instrumentality must conform. *Roan v. Connecticut Industrial Building Commission*, 150 Conn. 333, 341. Any rules or regulations which exceed statutory authority are void, however. *Berlinski v. Ouellette*, 164 Conn. 482, 492, Note. The statutory authority of the PUCA is copiously outlined in Connecticut General Statutes § 16-1 et seq. The rule making power is delineated in § 16-6b.[1]

[1] Sec. 16-6b. The division of public utility control . . . may . . . adopt such regulations with respect to rates and charges, services, accounting

All of the water companies in these three actions are so-called Class A water companies and all are contesting the validity of amendments to regulations adopted by PUC, which amendments became effective January 1, 1972. These amendments being questioned are part of a Uniform System of Accounts which was established to ensure uniform and consistent accounting practices and procedures for all Class A water companies. Each company is required to conform to the Uniform System of Accounts in maintaining its books. Some type of uniform system has been operative for over fifty years.

These amendments required that upon the sale of utility property and plant, *including land and land rights*, be accounted for in the income statement of the company, rather than in the surplus account. The uniform system of 1964 and before the subject amendments directed that the losses or gains on the sale of land or land rights be charged to the surplus account unless a reserve therefor had been provided; which is not the case here.

The effect of placing the gains or losses in the surplus account was that the proceeds never entered into the determination of company income, but was charged directly to the earned surplus account (below the line) and could be used to pay out dividends or could be invested in additional plant facilities of property.

The effect of the amendments which ordered the placement of gains or losses from sale of land in the company income statement (above the line) is that that income may be used by the PUCA in determining the rates to be paid by the consumer or in reducing that rate. In simple terms, if it were placed below the line (surplus) it is available for stockholders. If it is placed above the line (income) it is available to benefit the ratepayers. Therein lies the struggle — shareholders versus ratepayers.

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practices, safety and the conduct of operations generally of public service companies subject to its jurisdiction as it deems reasonable and necessary.

It is noted that the vast majority of the subject lands fit no one particular pattern. Some have been included in rate bases and some have not. Some was acquired in the exercise of the right of eminent domain and some were not. Some lands were in the rate bases and subsequently withdrawn therefrom and some were not.

There are some common features however. The ratepayers paid the taxes on the land through payments for service. They also paid for improvements to the land for purposes in their interests. And all land, when entered into the rate making process, entered at the original purchase cost and remained that way.

THE ISSUE

The rate of return by a utility on its investment is based on common equity. The consumers are required through rate paying, to afford investors a reasonable return on their investment. If a parcel of land is entered into the rate base, it is at original cost and the ratepayer has to pay a reasonable return for the use of that property. He never pays at the appreciated value of the land.

While other parts of the utility plant are depreciable, land is not. The ratepayer pays for the depreciation of plant in his payment for service. Since land is non-depreciable, the consumer never pays for it through his rates.

Plaintiffs maintain that the subject amendments to the accounting rules "interfere with, impair and threaten to interfere with the legal rights and privileges of the plaintiff by depriving them of their property without due process of law and by taking their property for public use without just compensation." They further contend that the inclusion by the PUCA of proceeds from the sale of land (and interest therefrom) is an abuse of the authority's statutory power and

> ". . . disregards the Authority's duty to approve rates which will (1) allow a fair and reasonable return on investment, (2) maintain [the company's] credit and

financial integrity, and (3) allow [the company] to attract needed capital and maintain the requisite level of services, and said error denies [the company] due process of law and equal protection of the law and constitutes a confiscation. . . ." See Connecticut General Statutes § 16-19e(a).

To be sure the Fifth Amendment to the United States Constitution provides that no person shall be deprived of his property without due process of law, nor shall private property be taken for public use without just compensation. The Fifth Amendment was made binding on the states by the Fourteenth Amendment, *Malloy v. Hogan*, 378 U.S. 1. And the issue here reduces itself to the question of whether the actions of the PUCA rises to a constitutional deprivation of property and whether the action is in deprivation of the statutory requirements imposed on it.

The issue is novel in this state. There are a few decisions in other states directly on point. In the course of these decisions, some have clearly articulated the reasons for the holdings. Some have stretched the holdings of antecedent cases.

The case which appears to have started and given life to public utility land sale cases is *Board of Commissioners v. New York Telephone Co.*, 271 U.S. 23. The court there made several statements which have been cited repeatedly by advocates of utilities. Some are:

> "Customers pay for service, not for the property used to render it. Their payments are not contributions to depreciation or other operating expenses or to the capital of the company. By paying bills for service they do not acquire any interest, legal or equitable in the property used for their convenience or in the funds of the company." at 32
>
> And
>
> "Constitutional protection against confiscation does not depend on the source of the money used to purchase the property. It is enough that it is used to render the service." at 31

This language has been seized on as representing the proposition that a public utility regulating agency cannot,

under any circumstances, consider proceeds from the sales non-depreciable land in its rate making function. Of course, *New York Telephone* does not so hold. There the Supreme Court had before it the question of whether consumers could benefit from excessive depreciation taken by the utility company in prior years, through an offset which would result in lower future rates. The court held that excess in the reserve for depreciation could not be used to make up the deficiency in current rates which made them confiscatory and not yielding a fair return.

There is no doubt that a public utility is entitled to a just compensation and that

> "The just compensation safeguarded by the Fourteenth Amendment is a reasonable return on the value of the property used for the public service. And rates not sufficient to yield that return are confiscatory. *New York Telephone* at 31."

The majority of the courts which have considered the issue have leaned heavily on the system of accounts used by the rate setting authority. The New Hampshire Supreme Court leaned on the *system* used when it said

> "Under the system of accounts presented by the Commission as well as matter of general equity, the net profit belonged to the stockholders. If the [electric generating plant] had been sold at a loss, the deficit could not have been charged to future consumers. By the same token a profit cannot be awarded to future consumers. *Chicopee Manufacturing Co. v. Public Service Co.*, 93 A.2d 820, 826 (1953)."

Plaintiffs have cited *Pennichuck Water Works v. State*, 164 A.2d 669 (N.H.) because it held that profits from land belonged to the general stockholder. They failed to note that *Pennichuck* relied on *Chicopee*.

Another case in the same vein is the *City of Lexington v. Lexington Water Company*, 458 S.W. 2d 778 (Ky) 1970. In that case the systems of accounts used was crucial. It said:

> "Under that system it was provided that a loss upon the sale of land is charged directly to the surplus ac-

> count — to the shareholders. A profit is credited in the same manner. The water company followed this accounting system." at 779.

The court appears to be saying that risk of gain follows risk of loss. And where, under the accounting system, the consumers could not be charged with any losses on the undepreciable land, he could not partake in any benefits.

Lexington went on to distinguish between it and *New York Water Service Corporation v. Public Service Commission*, 208 N.Y.S. 2d 857 (1960) (Appellate Division). The distinction was stated as follows:

> "That case can readily be distinguished because of the difference in the accounting methods. The New York Public Service Commission had adopted a system of accounts in which the land sold at a loss was debited to the depreciation reserve account and land sold at a profit was credited to that account. The New York court held that the rate base was thus properly increased or reduced affording the company protection from a loss in the sale of land used on the operations, therefore it was proper to pass profits made thereby onto the consumers." *Lexington* at 779.

Indeed *New York Water Service Corp.* did so hold. Therein, the gain or loss under the accounting system was on the consumers. In *Lexington* the gain or loss was on the shareholders or the utility.

Boise Water Corp. v. Idaho Public Utility Commission, 578 P.2d 1089 (Idaho) (1978) is the only case which appears to support plaintiff's position here, and it cites *City of Lexington v. Lexington Water Co.*, discussed above, as its authority. However, the opinion appears to be additionally based on the fact that ratepayers do not pay depreciation on land, it being non-depreciable. The type of accounting system used in *Boise* does not appear, and the court did not consider it.

The longest opinion (72 pages) and the opinion which collates every case touching on the subject of utility land sale and the problem presented here and gives the most

thorough discussion of the issue is *Democratic Central Committee of D.C. v. Washington M.A.T. Commission*, 485 F.2d 786 (1973) Cert. Den. 415 U.S. 935. In summing up its view of the numerous court decisions reviewed, the majority of that court concluded at page 798 that the decisions cannot be viewed as holding that capital gains on non-depreciable property inevitably belongs to the investors and may be accepted as applications of the broader principle *that the benefit of a capital gain follows the risk of capital loss*:

> "We cannot accept the thesis that appreciation in value . . . while in operating status automatically flows to [the] investors as inseparable incidents of ownership. *Democratic Central* at 805.

Democratic Central agrees that higher risks warrant a higher return but sees no risk involved in land, noting that historically land values have risen and any risk of financial loss has almost totally been foreclosed by the upward market. It opines at 811 that it is abstract logic to invoke "gain follows loss" where the risk of loss is wholly illusory as intended. In a separate opinion which concurred in the result and dissented in the rationale of the majority, Judge MacKinnon concludes that his reason for supporting the result reached by the majority was based on utility commission rules and regulations.

> "There enters another powerful judicial doctrine — that of deference to agency adherence to rules promulgated under statutory authority unless *arbitrary* or *capricious*. Again the ultimate question is whether the equities of the situation are so overwhelming that we can say that the Commission's *adherence* to its uniform system of accounts and its uniform administrative pronouncements was clearly arbitrary and capricious under the circumstances." *Democratic Central* at 844.

He further opines:

> "Clearly if the [Washington M.A.T. Commission] were to adopt an accounting procedure like that employed in N.Y. Water Service we would uphold its decision . . . ."

As previously discussed, the Commission in *New York Water* in its accounting procedures directed how a loss or gain from the sale of land should be treated — that is credited to the depreciation reserve; above the line.

ACCOUNTING METHOD PRESCRIBED BY THE PUCA

The PUCA adopted a regulation effective January 1, 1972 whereby gains and losses from the sale of land were to be carried "above the line." The effect of this was that the ratepayers would gain or lose from the sale. The shareholder would not.

Deference is given to a commission's treatment of accounting problems, notwithstanding some incidental intrusion on management prerogatives. *Northwestern Electric Co. v. Federal Power Commission,* 321 U.S. 119, 123, 124. The commission was not bound by the traditional concepts of business accounting. Legislative grants of administrative authority on utility accounting are designed to meet needs for information and the public need for economical rates so that inflationary writeups and expense padding may be avoided. *American Telephone & Telegraph v. United States* 299 U.S. 232, 277, 239-40. The supervision of accounting falls in the class of administrative action and in "gauging rationality" regard must steadily be had to the ends that a uniform system of accounts is designed to promote. *A.T.T.* at 237. However, a reviewing court must assure itself that the accounting practice prescribed is consistent with underlying substantive principles of public utility law. *New York Edison Co. v. Maltbie,* 281 N.Y. 223, 226. Affirmed 271 N.Y. 103.

> "This court is not at liberty to substitute its own discretion for that of administrative officers who have kept within the bounds of their administrative powers. *To show that these have been exceeded in the field of action here involved, it is not enough that the prescribed system of accounts shall appear to be unwise or burdensome or inferior to another. Error or unwisdom is not the equivalent of abuse. What has been ordered must*

> *appear to be so 'entirely at odds with fundamental principles of* correct accounting' (*Kansas City Southern Ry Co. v. United States,* 231 U.S. 423, 444) *as to be the expression of whim rather than the exercise of judgment." American Telephone* at 236, 237. (emphasis added)

An even if the PUCA adopted a uniform accounting system which was not in accord with the "best accounting methods" it is not for the court to determine what is the better practice so long as the commission has not plainly adopted an obviously arbitrary plan. *Northwest Electric Co. v. F.P.C.,* 321 U.S. 119, 124.

Moreover, the commission's Uniform System of Accounts does not become suspect because it is challenged.

> "It is the product of expert judgment which carries a presumption of validity. And he who would upset the [system of accounts] carries the heavy burden of making a convincing showing that it was invalid because it is unjust and unreasonable in its consequences." *Federal Power Commission* v. *Hope,* 320 U.S. 591, 602.

If the *total effect* of the accounting system cannot be shown to be unjust and unreasonable, then judicial inquiry is at an end. See *Hope* at 602.

The investor has an interest in the financial integrity of the utility and there should be enough revenue not only for operating costs but also for capital costs of the business and expansion. This includes debt service and dividends on stock. And the return should be sufficient to assure financial integrity of the utility so that it can attract capital and maintain a sound credit rating. *Hope* at 603.

When the rate of return authorized by the PUCA is sufficient to satisfy these criteria, it has satisfied both the statutory and constitutional criteria by which it is bound. The ratepayers never were the owners of the land. Nor were the shareholders ever the owners of the land. If, by some quirk, the utility company was ever dissolved, pro-rata division of the assets would be accorded the stockholders available above liabilities. This does not mean, however,

that the PUCA cannot give consideration to all of the utility equipment when it considers setting an adequate rate of return. If the rate is adequate to satisfy the statutory and constitutional standards, its duty is done.

The PUCA is auhorized and required to set up a Uniform System of Accounts. It has had one since 1922 and has changed it several times since then. Certainly there is no prohibition against changing the accounting system. And there is no prohibition against alterations in the "above the line" and "below the line" categories.

Most cases say that if the shareholder assumes the risk of loss, he should benefit from any gain; that he should not be put in the position of having to undergo risks if he is not to share in any gain. It would be anomalous if he were to take all the risks and the consumers were able to take all the gain.

Two of the instant cases arose when PUCA, which had previously ordered the removal of gains from the earned surplus (stockholders) account and ordered them placed in the appropriate column of the operating account, considered these gains in the rate making process.

In PUCA's revised system of accounting, any risk of loss in regard to the land has been totally removed from the shareholders resulting from the sale of land and placed in the operating account where any loss or gain becomes a burden or benefit to the ratepayer. If "benefit follows burden" or "risk of gain follows risk of loss" has any legitimacy, its standards have been satisfied in the revised Uniform System of Accounts.

If this theory is not palatable as sound economic theory, then the statutory grants of authority to the PUCA authorizing it to set up an accounting system and to make appropriate periodic changes, can provide the basis for its action. Working in tandem, it would appear that the action of the PUCA is supportable legally.

> "The Constitution does not bind rate-making bodies to the service of any single formula or combination of formulas. *Agencies to whom this legislative power has*

> *been delegated are free, within the ambit of their statutory authority, to make pragmatic adjustments which may be called for by particular circumstances. Once a fair hearing has been given, proper findings made and other statutory requirements satisfied, the courts cannot intervene in the absence of a clear showing that the limits of due process have been overstepped.* If the commission's order, as applied to the facts before it and viewed *in its entirety,* produces no arbitrary result, our inquiry is at the end." *Federal Power Commission v. Natural Gas Pipeline Co.,* 315 U.S. 575, 586 (emphasis added)

While the court in the above quotation was referring to rate making, the observations made therein are just as applicable to the setting up of a system of uniform accounts.

The requirements of the amendments to the Uniform System of Accounts which produced the results complained of here is well within the PUCA's discretion in working out the "balance of interest" here involved, *Federal Power Commission v. Texaco, Inc.,* 417 U.S. 380, 392 and is valid unless the affect is outside the *"zone of reasonableness"* in view of the public interest which the PUCA must keep in mind. *Permian Basin Rate Cases* 390 U.S. 747, 797. *Federal Energy Regulatory Commission v. Pennzoil Producing Co.,* — U.S. —; 99 S.Ct. 765, 772 (1979).

It has been aptly said and repeated by several courts that

> "Regulation may, consistently with the Constitution, *limit stringently* the return recovered on an investment, for investors interests provide only one of the variables in the constitutional calculus of reasonableness." *In re Permian Basin,* 390 U.S. 747, 769. *Bowles v. Willingham,* 321 U.S. 503, 518 (emphasis added)
>
> And
>
> A state has an interest in balancing consumer and investor interests and such a course is constitutional." *Permian Basin* at 769, 770.

The conclusion of the court is that (1) the PUCA was within its authority in adopting the amendments to the Uniform System of Accounts which had the effect of giving consideration to the proceeds of land sales in the rate

making process, (2) that its actions were neither arbitrary, capricious or illegal (3) that there was no violation of the Fifth and Fourteenth Amendments to the Constitution, due process and notice being adequate and that (4) there was no confiscation of property without great compensation. The plaintiffs have failed to carry their heavy burden of proof that the system of accounts was illegal, arbitrary or capricious, or that the PUCA's action was statutorily or constitutionally invalid. There was no showing that the rate of return on investment was inadequate, nor insufficient to attract investors.

For the foregoing reasons the following orders may enter in the following cases:

In No. 108038 *Greenwich Water Company, et als. v. Connecticut Public Utility Commission, et als.*, a declaratory judgment may enter that Sections 7, 411.6 and 411.7 of the Uniform System of Accounts are legal and valid regulations.

In No. 117874, *Bridgeport Hydraulic Company* v. *Public Utility Control Authority, et. al.,* the appeal is *dismissed.*

In No. 015775 *Litchfield Water Company v. Public Utility Control Authority,* the appeal is *dismissed.*

/s/ ....., J.
Graham, J.

NO. 108038

Greenwich Water Co., et al
vs
Howard E. Hausman, et al

NO. 117874

Bridgeport Hydraulic Company
vs
Public Utilities Control Authority, et al

NO. 015775

The Litchfield Water Company
vs
Public Utilities Control Authority

SUPREME COURT

STATE OF

CONNECTICUT

July 24, 1979

ORDER DENYING CERTIFICATION

The plaintiffs, Bridgeport Hydraulic Company and The Litchfield Water Company, having filed a petition for certification and the court having considered said petition finds that it should be denied.

Whereupon it is ordered that said petition be and it hereby is denied.

BY THE COURT

/s/ Thomas H. Abraham
Thomas H. Abraham, Clerk

No. 108038
Greenwich Water Co., Et Al
vs
Howard E. Hausman, Et Al

No. 117874
Bridgeport Hydraulic Co.
vs
Public Utilities Control
Authority, Et Al

No. 015775
The Litchfield Water Co.
vs.
Public Utilities Control
Authority, Et Al

SUPREME COURT
STATE OF CONNECTICUT
September 19, 1979

ORDER

The Motion of the petitioners, Bridgeport Hydraulic Company and The Litchfield Water Company, for Reargument and Reconsideration of Petition for Certification for Review and Request for Oral Argument having been presented to the court
it is hereby

ORDERED Denied.

By the Court,

/s/ Ronald P. Sherlock
Assistant Clerk of Supreme Court

NO. 9651 and 9652
Greenwich Water Co., et al
vs.
Howard E. Hausman, et al

SUPREME COURT
STATE OF CONNECTICUT
October 2, 1979

ORDER

The motion of the defendant, Division of Public Utility Control, to dismiss the joint appeal of the Greenwich Water Co. and the New Haven Water Co.; and the joint appeal of the Bridgeport Hydraulic Co. and the Litchfield Water Co. having been heard by the Court, it is hereby

ORDERED by the Supreme Court, that said motion be and the same is hereby granted.

By the Court,

/s/ Ronald P. Sherlock
ASSISTANT CLERK OF
SUPREME COURT

NO. 108038

GREENWICH WATER CO., ET AL
vs.
HOWARD E. HAUSMAN, ET AL

SUPERIOR COURT
J.D. OF HARTFORD AT HARTFORD
NOVEMBER 20, 1979

NO. 117874

BRIDGEPORT HYDRAULIC COMPANY
vs.
PUBLIC UTILITIES CONTROL AUTHORITY, ET AL

SUPERIOR COURT
J.D. OF FAIRFIELD AT BRIDGEPORT
NOVEMBER 20, 1979

NO. 015775

THE LITCHFIELD WATER COMPANY
vs.
PUBLIC UTILITIES CONTROL AUTHORITY

SUPERIOR COURT
J.D. OF LITCHFIELD AT LITCHFIELD
NOVEMBER 20, 1979

NOTICE OF APPEAL TO THE SUPREME COURT OF THE UNITED STATES

Notice is hereby given that Bridgeport Hydraulic Company and The Litchfield Water Company, defendants — cross complainants in No. 108038 and, respectively, plaintiffs in Nos. 117874 and 015775, hereby appeal to the Supreme Court of the United States from the final judgment of the Superior Court in No. 108038 declaring that Sections 7, 411.6 and 411.7 of the Uniform System of Accounts are legal and valid regulations and in Nos. 117874 and 015775, dismissing the appeals, entered in these actions on May 12, 1979.

This appeal is taken pursuant to 28 U.S.C. §1257(2).

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Filed Nov. 21, 1979
Superior Court, Judicial District of Hartford - New Britain at Hartford

Certificate of Compliance with Rule 33

This is to certify that a copy of the foregoing was served on the following, being all counsel of record, by depositing the same in a United States mailbox, first class postage prepaid, on November , 1979: Carl Burns, Esq., P. O. Box 191, 143 Rowayton Ave., Rowayton, CT 06853; Harold E. Drew, Esq., P. O. Box 470, Derby, CT 06418; Thomas E. DuPont, Esq., 23 Academy St., P. O. Box 267, Danielson, CT 06239; Richard P. Gilardi, Esq., 855 Main St., Bridgeport, CT 06604; Robert S. Golden, Jr., Esq., and William B. Gundling, Esq., Division of Public Utilities Control, State Office Building, Hartford, CT 06101; Joseloff, August & Sudarsky, 80 State St., Hartford, CT 06103; Joseloff, August & Sudarsky, 945 Hopmeadow St., Simsbury, CT 06070; Koskoff & McMahon, 144 West Main St., Plainville, CT 06062; Joseph C. Lee, Esq., Tyler, Cooper, Grant, Bowerman and Keefe, 205 Church St., New Haven, CT 06509; Maurice Maline, Esq., 65 Oak View Circle, Bridgeport, CT; Douglas McCallum, Esq., P. O. Box 176, Unionville, CT

06085; Pinney, Payne, VanLenten & Burrell, 26 West St., Danbury, CT 06810; Peter A. Treffers, Esq., P. O. Box 617, New Haven, CT 06509; Rural Water Company, Incorporated, West Redding, CT 06896; and Barry S. Zitser, Esq., Office of Consumer Counsel, Hartford, CT 06114.

Allan B. Taylor for
Day, Berry & Howard

DOCKET NO. 760701

APPLICATION OF
LITCHFIELD WATER COMPANY
TO INCREASE ITS RATES
TO ALL CUSTOMERS

DECISION

January 3, 1977

DECISION

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DECISION

I. INTRODUCTION

A. *Company Proposal*

By letter and application received July 6, 1976 The Litchfield Water Company filed with the Authority an amendment to its existing rate schedule, pursuant to Section 16-19 of the Connecticut General Statutes, as amended by Public Act 75-486, Section 8, which would increase its revenues on an annual basis by approximately $25,022 or 31.9%.

B. *Hearings Held*

In order to assist the Authority in its investigation, the matter was assigned for a public hearing. The public hearing was held in the Authority's hearing room in Hartford on October 18, 1976. Notice of the proposal and the public hearing was given to the Company, the Board of Selectmen in the Town of Litchfield, and to such other parties in interest as deemed necessary by the Authority. Public notice was given by advertisement in the Torrington Register, a newspaper having circulation in the area affected.

C. *Parties and Intervenors*

Pursuant to Sections 16-2(c) and 16-8 of the General Statutes, two Commissioners conducted the hearing. At the hearing, the applicant appeared by its President. There were no intervenors at the hearing.

Pursuant to Section 4-179 of the General Statutes, the applicant has agreed in writing to waive the reading of the record by a majority of the Authority.

II. APPLICANT'S EVIDENCE

A. *General*

The Company supplies water to about 707 metered customers in the Borough of Litchfield and part of the Town of Litchfield outside the Borough. The source of supply consists of two well fields. The Goshen well field consisting of three wells has a safe daily yield (SDY) of 200,000

gallons. The Hamill well field has one well with a SDY of 125,000 gallons. The total SDY equals 325,000 gallons. The average daily production during the test year was 243,600 gallons.

The transmission and distribution system consists of about 17.3 miles of 1″ to 8″ diameter cast iron, wrought iron, copper and ductile iron water pipes. There are two standpipes with a total water storage of 420,000 gallons.

The Company provides public fire protection through 81 hydrants and private fire protection through 10 private fire service lines.

B. *Rates and Revenues*

According to the Company's application, the present rates would be increased uniformly to all classes of customers, which would increase annual revenues by approximately $25,022.

A typical residential customer with a ⅝″ water meter using 18,000 gallons of water per quarter would be increased on a quarterly basis from $17.82 to $23.50.

C. *Finance and Test Year*

The Company last applied for and was granted rate relief in Docket No. 11287 dated September 27, 1972.

In the instant application, the Company claims that for the test year ended December 31, 1975, it experienced a net loss of $1,369. For a pro forma period at the present rates, a net loss of $1,453 would be experienced. At the proposed rates requested, the Company indicated that net income would be $16,614.

III. AUTHORITY ANALYSIS AND EVALUATION OF EVIDENCE

A. *Rates and Revenues*

To support its pro forma revenue exhibits, the Company submitted a detailed bill analysis of all its metered customers. This analysis determined the consumption in each rate block for the residential and commercial customers. The witness testified that there are no industrial customers

and that the public authority premises were included in the commercial classification.

Since we consider public authority facilities to be a separate classification, we shall therefore order below that as a condition to its next rate increase application, the Company shall list all public authority customers or facilities as a separate classification in the bill analysis and revenue exhibits. In addition, we shall expect that the Company to list its public authority revenue separately, as required, in its 1976 annual report.

In addition to the bill analysis the Company submitted a revenue adjustment to annualize for new customers added during the test year. Our review of the pro forma revenue adjustments made for the residential customer and the laundromat are acceptable as developed. We note, however, that the Company made no adjustment for the additional revenue it would receive from an elderly housing project completed in early 1976. Based on 1976 consumption data submitted by the Company, we therefore adjust upwards the company's pro forma revenues at the present rates by $551 and at the proposed rates by $727.

Subsequent to the test year the Company installed 1,500 feet of 8″ water main to parallel a 4″ main on East Street. The three hydrants located on the old 4″ main are to be removed and replaced by new hydrants on the 8″ main. Since the Company charges higher rates for public fire hydrants on water mains 6″ or larger in diameter we therefore increase pro forma revenues at the present rates by $225 and at the proposed rates by $297.

The total upward adjustment of pro forma revenues at the present rates is $776 and $1,024 at the proposed rates.

B. *Public Fire Protection*

It was determined through cross-examination of the Company witness at the hearing that the Borough of Litchfield pays the public fire protection charges for public hydrants located within the Borough. Outside of the Borough, however, the Town of Litchfield does not pay the public fire

protection charges. Here the Company must bill the public hydrant charges directly to the customers who live within a 500 foot radius of the public hydrants. This charge, which varies among the customers because it is determined by the number of customers located within 500 feet of each hydrant, has been added as an itemized portion of these customers' regular water bills.

We do not believe that the regular non-Borough water customers should also have to pay for public fire protection directly. A more satisfactory approach would be for the Town or Borough of Litchfield to assume this responsibility. In a similar situation involving a sister company, the Lakeville Water Company, we stated in our Decision to Docket No. 11794, that since people who live beyond a 500 radius of a hydrant also receive some benefits as to fire protection, these people should share in the costs of these hydrants. We expect the Company therefore to pursue this matter with the Town to arrive at a more equitable solution to the problem. In the interim, this method of charging for fire protection to non-Borough customers shall continue.

C. *Service*

The Company witness testified that, based on recent experience, the Company would probably continue its very slow growth rate in the foreseeable future and that the present well supplies would be adequate for about 10 more years. He stated also, that the Company had another well site available in the Hamill Well Field that will be developed when needed.

The Company acknowledged at the hearing, that although no specific complaints had been made regarding available fire flows or water service in general, the Company had contracted an engineering consultant to assess the Company's fire flow capabilities and recommend improvements where needed. This particular study concentrated on service in the area of West Street (Route 25) west of Milton Road. Thus far, the Company has installed two of the three sections of water mains recommended in Phase I of that report. The Company anticipates installation of the

third section of water main in the near future and completing Phases II and III as funds are available.

D. *Expenses and Authority Adjustments — Table I*

The Authority is of the opinion that authorized rates should be predicated upon reasonable and normal costs of operation. Thus, a test year selected by an applicant in accordance with Section 16-1-54 of the Administrative Rules of Practice, and adjusted for pro forma purposes, should contain expenses which are reasonable and can be considered to be representative of conditions which will prevail in the immediate future when the proposed rates are in effect.

Subsequent to the filing of the original application, the Company deemed it necessary to adjust certain of its proposed pro forma expenses, from those originally requested, in order to reflect known changes which were incurred by the Company since the original filing of its application. The changes representing additional increases or decreases in expenses are as follows:

Operating Expenses, net increase	$ 186
Payroll Taxes, net increase	13
Property Taxes, net increase	341
Other Income Deductions, net decrease	2,443

The Authority has reviewed the above items and finds that they are reasonable and proper to be included in the pro forma test year and therefore reflects the items in the "Authority Adjustments" column of Table I.

In our review of the Company's testimony and a field audit of its books and records, we find that the pro forma expenses claimed, with the following exceptions, are acceptable for determining the Company's revenue requirements at this time.

At the end of the test year, the Company's advances from its parent (Bridgeport Hydraulic Company) amounted to $65,500, which are in turn financed through the parent's short-term notes bearing current interest rates of 7.0% and 7.25%. For pro forma purposes the Company proposes an

interest charge of $5,732 using an 8.75% rate. Authority review of a requested late-filed exhibit indicated that the present short-term average interest rate being paid by the parent is 6.83%. By applying the 6.83% rate to the short-term debt of $65,500 outstanding at the end of the test year, the Authority calculates a pro forma interest expense of $4,474 which it considers proper for purposes of this rate application. We therefore disallow $1,258 of interest expense as proposed by the Company.

Prior to 1974 the original cost of $44,347.21, for the land and construction of a reservoir in Goshen, Connecticut, was recorded in the Company's books as Utility Plant in Service, Account No. 101. Per the Company's 1974 statutory report, the cost of the land and reservoir was transferred to Account No. 121, Non-utility Property, since the plant was reported to be no longer used in utility operations and available for sale.

Subsequent to the test year, the Company sold the reservoir including approximately 256 acres of land and reflected a gross sales price of $205,000. The Authority's examination of a requested late-filed exhibit, to show the effects of the entire sales transaction, revealed that the Company reflected a Connecticut Gross Earnings tax liability of $10,250 by applying the current 5% tax rate against the gross sales price of $205,000. Since the gross selling price of $205,000 is not subject to the Connecticut Gross Earnings Tax, the Authority has recalculated the related income taxes on this sales transaction. Per our calculation, the net profit before legal fees totals $108,933.

According to the Uniform System of Accounts prescribed for Class "A" Water Utilities, Account No. 256 — Deferred Gains from Disposition of Utility Plant, states "This account shall include gains from the sale or other disposition of property previously recorded in accounts 101-104, in account 105, Property Held for Future Use or Account 121, Non-utility Property, where such gains are significant and are to be amortized over a period of five years, unless otherwise authorized by the Commission. The amortization

of the amounts in this account shall be made by credits to Account 411.6, Gains from Disposition of Utility Plant or Account 421.1, Gain on Disposition of Property, as appropriate. Amounts recorded in this account shall be net of related income taxes." Because of the magnitude of the amount involved, the Authority deems it appropriate to amortize the net profit of $108,933 over a 7 year period. Therefore, we include in Account 411.6, Gains from Disposition of Utility Plant, the net amount of $15,562 for accounting and rate-making purposes. The requested late-filed exhibit indicated that the Company has utilized Account 256 in reflecting the sale of the subject property.

In conjunction with the land sale, the Company received from the buyer $41,000 in cash and accepted a 20-year Mortgage Note Receivable in the amount of $164,000, bearing an interest rate of eight percent (8%) per annum. Interest and principal shall be paid annually in the amount of $16,703.77. Based on the aforementioned facts, the Authority calculates that the Company will receive gross interest of $13,120 one year after the date of this Mortgage Note, resulting in net interest income after related income taxes of $7,942. We therefore increase pro forma interest income by $7,942 for purposes of this rate application.

The Company computed a pro forma federal income tax liability at the proposed rates amounting to $3,670 calculated on a separate return basis when, in fact, as a member of a holding company system it has, since 1970, participated in the filing of a consolidated federal tax return. The companies participating in the filing of a consolidated return become individually and severally liable for the tax liability; that is, the filing of a consolidated return does not produce any separate income tax liability on the taxable income of each participating company, but instead produces a tax liability for the group as a whole.

The Authority has consistently found in several Findings relating to rate applications of water utilities under its jurisdiction that utility customers of a participating company in a consolidated group should be required to pay no

more or less than the utility's allocated share of the system's actual tax liability.

Under the circumstances, the Company's proposal to reflect a pro forma tax liability on an individual basis is in conflict with the established regulatory principle that, since a utility's customers must reimburse it for all taxes paid, a utility must charge its customers for the amount of taxes paid or for its equitable share of a consolidated tax liability.

Because of fluctuations in the earned income of the several companies participating in the consolidated tax return, we believe the actual experience arising from filing on a consolidated basis over a representative period broad enough to offset peaks and valleys of individual years should be used in determining the average effective tax rate for pro forma purposes. From the exhibit requested by the Authority, the following tax liabilities actually existed:

Year	Taxable Income of Companies with Taxable Income	Consolidated Tax Liability	Authority Calculated Tax Liability	Authority Calculated Effective Tax Rate
1971	$2,272,091	$861,916	$	37.9%
1972	2,068,515	683,636		33.1
1973	2,480,343	887,873		35.8
1974	1,468,053	444,727		30.3
1975	1,734,181	445,883	*545,760	31.5

* The Authority has increased the consolidated tax liability by $99,877, to reflect the company's election for the normalization of the additional 6% Investment Tax Credit for accounting and rate making purposes, as required by the Tax Reduction Act of 1975.

The Authority is of the opinion that for pro forma purposes the average of the five-year rates or 33.7%, should be utilized in computing the Company's tax liability for purposes of the rate application. We will therefore consider 33.7% as a reasonable approximation of the estimated future effective tax rate.

The Authority calculates that at the proposed rates requested and after adjustments to expenses as detailed above, and utilizing the effective tax rate of 33.7%, the Company's tax liability on a consolidated basis would be $7,515 or $3,845 more than that proposed by the Company.

The Company computed a Connecticut State Business Tax of $2,085 calculated at the 10% rate as if it filed on a separate return basis. Effective with 1973, the Company has participated in the filing of a consolidated Connecticut State Business Tax return and the following was actually experienced:

Year	Taxable Income of Companies with Taxable Income	Consolidated Tax Liability	Authority Calculated Tax Liability	Authority Calculated Effective Tax Rate
1973	$2,480,343	$193,415	*$241,769	9.7%
1974	1,468,053	97,071	* 121,338	8.3
1975	1,734,181	139,960	139,960	8.1

* Recalculated to reflect increase in tax rate from 8% to 10%.

Since the privilege of filing the Connecticut Business Tax on a consolidated basis became effective in 1973, there is but a three year historical record available to the Authority upon which an average effective rate can be determined. As noted above, the Authority has recalculated the consolidated and the effective tax rates based on the current tax rate of 10% (formerly 8%) effective in 1975. We will therefore use the average of the three-year effective rates as adjusted, or 8.7%, which is a reasonable approximation of expected future operations. The Authority by applying the said 8.7% rate to the taxable income, as adjusted by us for pro forma purposes, calculates the tax to be $2,125 or $40 more than that proposed by the applicant.

Table I below, shows the pro forma income statement at the proposed rates as presented by the Company, the adjustments made by the Authority, and the pro forma as modified by the Authority:

Table I

	Pro Forma at Proposed Rates	Authority Adjustments	Pro Forma with Authority Adjustments
Operating Revenues:			
Present Rates	$ 78,409	$ 776	$ 79,185
Proposed Increase	25,022	248	25,270
Total Operating Revenues	$103,431	$ 1,024	$104,455
Operating Expenses:			
Operating and Maintenance	$ 42,638	$ 186	$ 42,824
Depreciation	8,794		8,794
Tax — Property	15,307	341	15,648
— Gross Earnings	5,227	51	5,278
— Conn. Business	2,085	40	2,125
— Federal Income	3,670	3,845	7,515
— Other	721	13	734
Gain — Disposition of Utility Plant	0	(15,562)	(15,562)
Total Operating Expenses	$ 78,442	$(11,086)	$ 67,356
Utility Operating Income	$ 24,989	$ 12,110	$ 37,099
Other Expenses	(2,643)	2,443	(200)
Interest Income		7,942	7,942
Income before Interest Charges	$ 22,346	$ 22,495	$ 44,841
Interest Expense	5,732	(1,258)	4,474
Net Income	$ 16,614	$ 23,753	$ 40,367

Our analysis of the evidence presented indicates that the net income the Company would realize at the proposed rates after payment of its operating expenses, taxes and depreciation would be $40,367 which is more than just, reasonable and necessary in order to enable the Company to maintain its financial stability and to provide adequate service.

IV. FINDINGS OF FACT

A. *Authority Allowed — Table II*

1. The test year for this rate application is the operating and revenue experience of the Company for the twelve months ended December 31, 1975, which we find is reasonable as a basis for the Company's application and is hereby accepted.

2. The present rates charged by the Company are just, reasonable and adequate to enable the Company to provide properly for the public convenience, necessity and welfare.

3. The adjustments made by the Authority in Table I are found to be appropriate.

4. The Company's net income, after Authority adjustments, as shown in Table I, is more than just and reasonable. The increase sought by the applicant in the proposed amendment to the existing schedule of rates on file is denied.

5. Table II, below, shows the revenues and expenses found reasonable by the Authority:

TABLE II

Operating Revenues:	
Present Rates	$ 79,185
Total Operating Revenues	$ 79,185
Operating Expenses:	
Operation and Maintenance	$ 42,824
Depreciation	8,794
Taxes — Property	15,648
— Gross Earnings	4,014
— Connecticut Business	36
— Federal Income	129
— Other	734
Gain — Disposition of Utility Plant	(15,562)
Total Operating Expenses	$ 56,617

Utility Operating Income	$ 22,568
Other Expenses	(200)
Interest Income	7,942
Income Before Interest Charges	$ 30,310
Interest Expense	4,474
Net Income	$ 25,836

6. Rates and revenues at this level are not unreasonably discriminatory or more or less than just, reasonable and adequate to enable the Company to provide for the public convenience, necessity and welfare.

V. CONCLUSION

A. *Summary*

Based on the foregoing, the amended schedule of rates as filed with the Authority is denied. The Company is directed to comply with the following conditions:

B. *Conditions*

1. The Company shall amortize the Authority adjusted deferred gains from disposition of property, reported by the Company as presently reflected in Account 256, over the next seven years. The amortization of $108,933 shall be made by credits to Account 411.6, Gains from Disposition of Utility Plant.

2. The Company shall, as a condition to a future rate increase application, include a public authority classification of customers in its detailed bill analysis and revenue exhibits. In addition, the Company shall list public authority revenues separately in its 1976 annual report.

3. The Company shall continue its efforts to persuade the Town or the Borough of Litchfield to assume the responsibility of payment for all public fire protection service provided by the Company and report to the Authority by June 1, 1977 the results of the negotiations.

(see next page)

We hereby direct that notice of the foregoing be given by the Executive Secretary of this Authority by forwarding true and correct copies of this document to parties in interest, and due return make.

Dated at Hartford, Connecticut this 3rd day of January 1977.

Albert J. Kleban)
)
Miriam B. Butterworth)
) PUBLIC UTILITIES
Gerald J. McCann) CONTROL AUTHORITY
)
Richard O. Jones)
)

State of Connecticut)
) ss. Hartford, January 3, 1977.
County of Hartford)

I hereby certify that the foregoing is a true and correct copy of Decision, issued by the Public Utilities Control Authority, State of Connecticut.

Attest:

/s/ Henry Mierzwa
Executive Secretary, Public Utilities Control Authority

This Commissioner dissents from the decision of the majority and is of the opinion that the effect of the majority decision will be: (1) to deny ratepayers due process and (2) to establish rates which are excessive, unjust and unreasonable.

Findings of this Commissioner will be issued separately in the near future.

Thomas K. Standish
Commissioner

Addendum to Majority Decision

A review of Commissioner Standish's statement indicating grounds for dissent requires additional comment by the majority.

At no time during the deliberative process were either of the dissenting allegations raised. There was never a question that due process had not been fully accorded consumers by our decision. In fact, Commissioner Standish himself conducted the hearings in the instant case and did not indicate any absence of due process, nor did he suggest that the rates retained as a result of the denial of the rate request were not properly established or that such rates were not just and reasonable.

Until this date (January 4, 1977) the only area of dissent made known to the other Commissioners by Commissioner Standish was the treatment of the net proceeds of the sale of land by the Company.

Albert J. Kleban

Miriam B. Butterworth

Gerald J. McCann

Richard O. Jones

Inasmuch as the majority have seen fit to comment upon the statement of this Commissioner wherein grounds for dissent are summarized, it is appropriate to respond under these unique circumstances. The statement of the majority in the *Addendum to Majority Decision* is entirely incorrect, without foundation and misleading to the public.

The extensive Findings of this Commissioner to be issued in the near future, will fully address these further issues raised in the *Addendum*.

Thomas K. Standish
Commissioner

EXPLANATION OF FINDINGS OF

Commissioner Thomas K. Standish
(Not a part of Findings)

The Decision of the majority will set rates which will be used to charge consumers for water service. It is found by Commissioner Standish that:

1. Because of the policies and methods used by the majority, the level of revenues which the Litchfield Water Company will collect will be excessive, unfair to consumers, and unreasonable according to established principles of regulation.
2. In order to adhere to an accounting procedure inherited from the old PUC, the majority have denied consumers the right to collect $170,075 over the next twenty years. This constitutes a "taking" of consumers monies contrary to constitutional and statutory protections.
3. The majority have granted the Company a rate of return which is excessive due to the $170,075 taken from consumers. This is a windfall profit to the investors of the Litchfield Water Company which is unfair and prejudicial to consumers.
4. The accounting policy followed by the majority is inconsistent and contradictory, granting consumers only part of the total gain to which they are entitled yet, at the same time, conceding the principle that consumers should receive gains from the sale of the Goshen Reservoir property.

Beyond the narrow question of the proper treatment of the proceeds and interest from the sale of the Goshen reservoir, the decision of the majority could set an undesirable precedent which will, at consumers expense, produce windfall profits for water company investors. If allowed to stand, the decision of the majority could result in millions of dollars of ratepayers monies being made available to water company stockholders at the time water company

lands are sold. This probable result follows from the fact that many water companies in Connecticut will be disposing of their reservoirs once filtration facilities are built to conform with the requirements of the Federal Safe Drinking Water Act of 1974.

The majority have granted the Litchfield Water Company one of the highest rates of return in the history of Connecticut regulation. These profits are the direct result of the improper treatment of gains from the sale of the Goshen reservoir property. Consumers should have been granted a substantial rate reduction to reflect the flow-through of monies which rightfully belong to them.

DOCKET NO. 770301

APPLICATION OF
BRIDGEPORT HYDRAULIC COMPANY
To Increase Its Rates To
All Classes Of Customers

DECISION

JUNE 30, 1977

DECISION

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DECISION

I. INTRODUCTION

A. *Company Proposal*

On March 1, 1977, pursuant to Section 16-19 of the Connecticut General Statutes, Bridgeport Hydraulic Company filed an application to increase its rates and charges to all classes of customers. The proposed increase is designed to produce approximately $2,841,000 per annum, or approximately 17.3 percent above the revenues produced by the present rate schedule. The effective date of the proposed rates is March 2, 1977.

As part of this proceeding, Bridgeport Hydraulic Company has requested the Authority:

(1) To approve a revision to its depreciation rates which would increase its annual composite rate from 1.76 percent in the test year to 1.85 percent in 1977, and 1.92 percent in 1978;

(2) To allow the inclusion in the rate base of construction work in progress related to the construction of filter plants required by The Safe Drinking Water Act;

(3) To allow full normalization of the timing differences between book treatment of certain items such as depreciation, investment tax credit, and various overheads and other charges related to construction.

B. *Hearing Held*

Pursuant to a *Notice of Hearing* dated May 2, 1977, a public hearing on Bridgeport Hydraulic's application was held in Bridgeport on May 16, 1977. The hearing was reconvened in Hartford on May 18, 19, 26, 27 and 31, 1977.

C. *Parties and Intervenors*

Bridgeport Hydraulic Company is the party in interest. The following have been recognized by the Authority as intervenors:

The Office of Consumer Counsel
The Town of Trumbull
The Town of Stratford
Mr. Joel Cohn
The Connecticut Consumer Group
The United Machine Workers of America
The Commission on Aging for the City of Bridgeport

The Authority has received letters pertaining to Bridgeport Hydraulic's application from the Town of Seymour and the City of Shelton. Letters were also received from concerned citizens served by Bridgeport Hydraulic.

II. APPLICANT'S EVIDENCE

A. *General*

1. *Company Witnesses*

Bridgeport Hydraulic Company presented the testimony of six witnesses in support of its application.

Mr. William S. Warner, President and Chief Executive Officer of Bridgeport Hydraulic Company, testified generally as to the Company's need for rate relief. Mr. Warner's testimony summarized the key issues addressed in the application.

Mr. Robert H. Reinert, Vice President of Engineering of Bridgeport Hydraulic Company, appeared before the Authority as the Company's engineering witness. Mr. Reinert's testimony dealt with the Company's projected water demands and safe yields, the present and proposed rate schedules, plant additions and capital expenditures.

Mr. Ronald J. Verrilli, Vice President of Finance of Bridgeport Hydraulic Company, appeared before the Authority as the Company's financial witness. Mr. Verrilli's testimony dealt with the Company's balance sheet, income statement, operation and maintenance expenses, inter-company charges, rate base and return on rate base, and the coverage of fixed charges.

Mr. Jay H. Price, Jr. of Arthur Andersen and Company, a firm of independent public accountants, testified on behalf of Bridgeport Hydraulic Company. The purpose of Mr. Price's testimony was to comment on Bridgeport Hydraulic's pro-forma adjustment to normalize income taxes. Mr. Price recommended that the Company be allowed to move toward normalization accounting and rate making.

Mr. Gordon V. Smith of Associated Utility Services, Inc. also testified on behalf of the Company. Mr. Smith's testimony dealt with depreciation accrual rates.

Mr. Joseph F. Brennan of Associated Utility Services, Inc. testified on behalf of the Company. The subject of Mr. Brennan's testimony was the rate of return, inclusion of construction work in progress in the rate base, and the financial considerations regarding depreciation practice with respect to impact.

2. *Reason for Request for Rate Relief*

The President and Chief Executive Officer of the Company testified that in order for the Company to be successful in raising the necessary capital to finance its construction program it must be able to demonstrate to prospective investors a satisfactory and consistent track record with respect to earnings on common equity and coverage of fixed charges on senior securities.

The witness stated that the Company has studied a number of alternatives, and will continue to make studies, in an attempt to accomplish the external financing which will be required over the next five years. The Company has also studied means of developing and maintaining the level of earnings from operations during the period required to support its financing. The witness further stated that in order for the Company to meet its objective, it must at this time demonstrate an ability to achieve and sustain satisfactory

earnings. Thus, it was claimed, rate relief is necessary in order to allow the Company to increase its return on equity to a level attractive to investors and to provide a reasonable margin over minimum fixed charge coverage requirements.

B. *Finance and Test Year*

The Company last applied for and was granted rate relief in Docket No. 11736 by a Decision dated November 25, 1975.

In the instant application, the Company claims that for the test year ending December 31, 1976, it experienced utility operating income of $5,013,000 and a rate of return of 8.3%. It was further claimed that a pro forma period at the present rates would reflect an operating income of $4,336,000 and a rate of return of 7.1%. At the proposed rates requested, the Company indicated that operating income would be $5,983,000 and that the rate of return would be 9.75%.

C. *Rate Structure*

The Company's witness testified that he would propose no basic changes in the rate structure at this time.

The witness sponsored an updated cost of service study (Exhibits 7 & 36) in connection with its application for a rate increase as directed by the Authority in Docket No. 11736.

He proposed to increase the metered minimum charge slightly more than the overall increase of 17.3% in order to bring the revenue derived from residential customers closer to the allocation factor for this class of service as shown in the cost of service study.

According to the Company's witness, residential customers are contributing less than their fair share of operating revenues as set forth in the cost of service study. Based upon the apportionment shown therein, residential customers' portion of total revenues should approximate 49.1%. Under the Company's proposal, residential customers' portion would be about 45.6%. The witness felt that a larger

increase at this time would be an undue burden on the residential customer.

The witness testified that fire protection service customers provided about 13.8% of total water revenues in the test year. Under the proposed rates they would contribute some 13.7% of total revenues.

The tabulation below, taken from Exhibit 7, summarizes the allocation of revenues between the several classes of service based upon the cost of service study and the percentage of total proposed revenues contributed by each group, as proposed by the Company's witness.

Class of Service	Per Study in Percent	Produced by Proposed Rates in Percent
Fire	12.3	13.7
Flat Rate	9.7	10.4
Residential	49.1	45.6
Commercial	13.2	14.1
Industrial	15.7	16.2
TOTAL	100.0	100.0

The witness stated that such studies were helpful as aids to judgment, to be weighed with other factors such as historical relationships between the classes of customers served, customer impact and public acceptability.

During the course of the hearings in Docket No. 761109, hearings in various matters affecting water companies in Connecticut, Bridgeport Hydraulic joined with New Haven Water Company in offering various concepts and innovations in water rate structures. The Company witness said that after the Authority's decision in that docket is issued, the Company would plan to move ahead with a study to determine Bridgeport Hydraulic's implementation.

D. *Rates*

According to the Company's application, percent rates would be increased, on average, by about 17.3% to produce additional annual revenues of approximately $2,841,000. The bill of a typical residential customer with a 5/8 inch meter and using 2,500 cubic feet per quarter would be increased on an annual basis from $88.80 to $106.24 or 19.3%. A metered residential customer using the minimum quarterly consumption allowance of 1,200 cubic feet would be increased on an annual basis from $56.04 to $68.52 or 22.3%. A typical flat rate customer would be increased on an annual basis from $84.40 to $97.08 or 15.0%. A private fire protection service customer served through a six-inch diameter fire line, would be increased from $237.38 per year to $273.03 per year or 15.0%. For public fire protection customers, the charge per inch foot would be increased by 14.8% while the annual charge for each Company owned hydrant would be increased by 15.7%.

E. *Revenues and Revenue Adjustments*

Operating revenues for the test year, the twelve months ending December 31, 1976, were $16,389,000 (Ex. 11, p. 1). Increases in revenue due to annualization of current rates amounted to $64,000 or a total of $16,453,000 and at proposed rates of $19,294,000.

F. *Construction Program*

The Company's vice president of engineering testified that the total projected capital budget for the years 1977 through 1981 would range from $4,000,000 in 1977 to over $9,000,000 in 1978, peaking at $11,700,000 in 1979, then decreasing to $10,600,000 in 1980 and to $6,100,000 in 1981. These amounts are net of contributions in aid of construction. Recurring capital additions of $3,000,000, chiefly mains, services, meters and hydrants, it was estimated, would be expended annually in 1977-1981.

The witness said the Trap Falls treatment project accounts for most of the capital budget between 1977 and 1981. The Far Mill and Trap Falls pipeline projects are part of changes in the Company's system required when the filter plant is constructed at Trap Falls.

Although waters from the Company's Hemlocks and Easton reservoirs currently meet the new federal and state standards prescribed under the 1974 Safe Drinking Water Act, the witness stated that the State Health Department

"has strongly indicated" that all surface supplies will require filtration.

He emphasized that the projected capital budget was not related to increased water use but rather reflected the need to implement the new water quality standards promulgated by the Federal Government and endorsed by the Connecticut State Health Department.

G. *Depreciation*

Annual depreciation is accrued on the Company's water plant service using straight line depreciation on the basis of various average service lives which it deems appropriate for the twenty-six plant accounts, each containing a specific type of property. Each such plant account has an associated depreciation rate. These rates currently range from 1% to 12.5% per year.

A consultant presented evidence regarding the depreciation rates, which he testified, should be adopted by the Company for use now and in the near future. The witness stated that such rates should be reviewed periodically.

In reaching his conclusions concerning the depreciation rates that the Company should adopt, the witness used the group method straight line depreciation. He explained that water plant items of similar retirement characteristics were grouped together and an average life for the group, not for any single unit within the group, was found. This method was similar to that used by actuaries of life insurance companies in studying human mortality data, according to the witness. He also inspected the various visible elements of the Company's property such as reservoirs, dams, pumping stations, treatment facilities, storage tanks, office buildings and related equipment and garages. More than 68% of the Company's depreciable plant such as mains, services and hydrant branches are underground. Schedule 1 of Exhibit 58 illustrates the application of the Company's current depreciation rates and those advocated by the witness. Using year end figures as of December 31, 1975, he calculated the overall composite depreciation rate,

using current practice at 1.76% and 1.78% based upon his rates. The witness claimed that his recommendations were appropriate for the present and the future.

Since depreciation expense did not represent a cash outlay by the Company (it was a source of internally generated funds) there were financial aspects of depreciation which must be explored and given appropriate consideration. The dollars accrued in the reserve for depreciation of water plant in service over the service lives of the utility property will equal the same number of dollars originally invested. However, the witness stated that the dollars so collected would purchase less new plant intended as a replacement.

The witness believed that there was a difference between the investor's view of the water industry's business and the estimated life of water plant property, viewed in the traditional manner. However, he did not recommend the recovery of any dollar amount, other than that set forth in the Company's books and records. That dollar amount would differ from a cost base. The witness testified that he recommended a faster recovery of said depreciation base, but only in an amount equal to the original cost net of salvage, if any.

While his proposed rates of annual depreciation would not produce recovery of more dollars than those originally invested over the service life of the property, his proposed change would "slightly speed up the rate of recovery of the moment to better accommodate the economic and financial facts of life of the moment" according to the witness.

On the basis of his study the witness proposed a composite rate of annual depreciation expense of 1.85% for the year ending December 31, 1977 and that said rate should be increased to 1.92% in 1978 and to 2.00% in 1979.

H. *Rate Base*

A discussion of the Company's rate base evidence has been incorporated in the Authority's Analysis and Evaluation of Evidence. See Section IV., F., *infra*.

I. *Financial Data*

1. *Cost of Money — Rate of Return — Attrition Allowance*

The Company presented evidence on the cost of money, rate of return and attrition allowance through an independent consultant. These exhibits, testimony and related data have been incorporated into the Authority Analysis of Cost of Money — Rate of Return — Attrition Allowance. See Section IV., G., 1., *infra.*

2. *Normalization vs. Flow Through of Income Taxes and Service Life Method vs. Initial Year Flow Through of Job Development Credit*

The Company presented evidence on the treatment of all timing differences between book and tax depreciation, as well as the permanent savings of the job development credit service life method and full normalization of the investment tax credit through an independent consultant. These exhibits, testimony and related data have been incorporated into the Authority Analysis of these issues. See Section IV., G., 2., *infra.*

J. *Construction Work in Progress*

In this proceeding the Company seeks the inclusion in rate base of construction work in progress (CWIP) of $324,000, reflecting costs incurred to date on its Trap Falls project. The Company witness stated that no interest would be capitalized on that portion of construction work in progress included in rate base.

If construction work in progress is not included in rate base, the Company is forced to continue to use a "less desireable alternative", namely, capitalization of an allowance for funds used during construction (AFUDC), its witness contends. Since the Trap Falls project has an estimated cost of $14,000,000 spanning several years, an ever increasing percentage of reported net income would consist of AFUDC which investors are said to view with disfavor since such earnings do not represent cash earnings. He

further stated that, in his opinion, the Company would experience an impairment of its credit as AFUDC increased as a percentage of operating income.

K. *Expenses*

The testimony and exhibits offered by the Company's Vice President of Finance detail the Company's proposed expenses. The Company's pro forma expenses are discussed, and adjusted where necessary, in the Authority's Analysis and Evaluation of Evidence. See Section IV., I., *infra.*

III. INTERVENORS' POSITIONS

A. *The Office of Consumer Counsel*

The Office of Consumer Counsel participated in the cross-examination of Company witnesses and presented expert testimony in opposition to Bridgeport Hydraulic Company's application. Mr. Edgar H. Bernstein and Mr. Jatinder Kumar, both of Associated Regulatory Consultants, Inc., testified on behalf of the Office of Consumer Counsel.

1. *Construction Work in Progress*

The Office of Consumer Counsel is opposed to including construction work in progress in the rate base. One of the witnesses for the Office of Consumer Counsel said that inclusion of construction work in progress relating to the Trap Falls project would result in an additional $54,990 in revenues annually over and above the present costs of service, for future facilities not in service or of use to them. He claimed that normal and current procedure should be for the Company to capitalize an allowance for funds used during construction which recognizes a return of CWIP to be paid through depreciation expense by those customers using the facilities when it is placed in service. The witness added while the amount sought herein is small ($324,000) the Company was "trying to establish a principle. Once one portion of CWIP is includ-

ed in rate base, the next step is to include all CWIP in the rate base".

He contended that the customers would pay an additional $4,712,493 whereas, according to his calculations, the present value of AFUDC in rate base would be $1,474,276 using a rate of return of 9.3%. He concluded that excluding CWIP from rate base and capitalizing AFUDC on the construction expenditures is much less costly to the ratepayer than putting CWIP in the rate base at this time. The witness pointed out that AFUDC in 1976 represented 1.9% of utility operating income. The stockholder is not penalized since accumulating AFUDC only causes a difference in timing as to when the stockholders earn a return on his investment in water plant, namely, when plant is placed in service for the rendition of water service, according to the witness. In his view the policy adopted in Docket No. 760604 — Application of Connecticut Light and Power Company to increase its electric and gas rates to all customers, Decision, December, 1976, wherein the Authority disallowed CWIP in rate base should be applied in the subject Docket.

2. *Normalization vs. Flow Through Accounting For Certain Tax Benefits*

The Office of Consumer Counsel is opposed to Bridgeport Hydraulic Company's proposed change from the flow through method of accounting to the normalized method of accounting for timing differences related to the tax consequences of accelerated depreciation and the investment tax credit. One witness for the Office of Consumer Counsel was opposed to normalization for the following reasons:

"(1) This process results in an increase in costs to the ratepayers which is not related to any increase in the Company's costs.

(2) Normalization of taxes results, if not in permanent tax savings, at least in a mismatch of revenues and actual costs.

(3) The ratepayers would be required to pay approximately two dollars of revenue for every one dollar of deferred tax expenses.

(4) Normalization results in requiring the ratepayers to make involuntary contributions to the capital of the utility.

(5) Normalization may result in a permanent tax savings for a majority of the utility companies.

(6) Normalization does not result in increased reported earnings and after-tax coverage ratios.

(7) Flow through, not normalization, produces equity between current and future operations."

3. *Other Issues*

The Office of Consumer Counsel has also expressed its position on five additional issues. It is the Consumer Counsel's position that the proposed depreciation rates are not based on sufficient evidence to warrant their imposition. It is also the Consumer Counsel's position that the pension for Mr. D. C. Warner should be disallowed and that expenses related to officers' business expenses should be examined by the Authority and be disallowed if not appropriate. The Consumer Counsel believes that the proposed adjustment to payroll expenses should not be allowed. Finally, the Consumer Counsel recommends that the Authority examine the operation of the Aspetuck apple orchard which is operated by Bridgeport Hydraulic Company. The Consumer Counsel is concerned about the profitability of this operation and the possibility that consumers might be charged for losses resulting from this operation.

B. *Mr. Joel Cohn*

Mr. Joel Cohn made a statement to the Authority as a shareholder of the Hydraulic Company (the parent company of the Bridgeport Hydraulic Company). Mr. Cohn was in favor of the proposed rate increase but recom-

mended that the Authority investigate the operation of the Hydraulic Company and the Bridgeport Hydraulic Company. Mr. Cohn recommended that the Authority require greater efficiencies on the part of Bridgeport Hydraulic and that the Company's operation be clearly separated from the Hydraulic Company.

C. *Town of Trumbull*

The Town of Trumbull opposed Bridgeport Hydraulic's proposed rate increase. It respectfully requested that any action taken by the Authority to implement a rate increase be effective and coincide with the appropriate budget-making processes of the various communities served by Bridgeport Hydraulic. Trumbull is on a July 1st fiscal year and has established its new fiscal mill rate through June 30, 1978. The Town of Trumbull is aware of the deferrals granted by Connecticut General Statutes, Section 16-19(e) but the Town believes that such deferrals are inadequate.

D. *Town of Stratford*

The Town of Stratford objected to the size of the proposed rate increase. The Town believes that the proposed charges for its fire service is excessive. The Town and its residents also believe that they should not have to bear the capital cost for the Company's extension into new undeveloped areas of surrounding towns. The Town stated that since the owners of the Company share in profits they should also share in the burden of raising capital. The Town of Stratford urged that Bridgeport Hydraulic scrutinize its budget for all possible cost savings.

E. *Commission of Aging for the City of Bridgeport*

The Commission of Aging for the City of Bridgeport is concerned that the proposed rate increase would place an added burden on elderly citizens who are property owners. Elderly persons living on fixed incomes and savings could be forced to consider selling their homes and using their savings. The Commission requested that Bridgeport Hydraulic be concerned and sensitive to the needs of the elderly who have difficulty in meeting rate increases.

F. *The Connecticut Consumer Group and The United Machine Workers of America*

Mr. Albert Cioffari made a statement on behalf of the Connecticut Consumer Group and The United Machine Workers of America. Mr. Cioffari stated that the proposed rate increase would be an additional burden on those persons living on fixed incomes. Mr. Cioffari was concerned about losses suffered by a subsidiary of the Hydraulic Company. He believes that the Authority should evaluate the activities of the Hydraulic Company in making its decision on Bridgeport Hydraulic's proposed rate increase.

G. *Others*

The Authority received a letter on behalf of the Town of Seymour. The Town opposes the proposed rate increase as an increased burden to its taxpayers. The Town believes that if Bridgeport Hydraulic needs increased earnings such earnings should be the result of improved efficiency rather than higher rates.

The Authority also received a letter on behalf of the City of Shelton. The City is opposed to the rate increase because it adversely affects its citizens. The City believes that current water rates are too high and that the proposed increase is unjustified.

Letters received from various concerned citizens express opposition to the proposed rate increase.

IV. AUTHORITY ANALYSIS AND EVALUATION OF EVIDENCE

A. *Test Year*

The Authority has analyzed the test year utilized by the applicant, and finds that it is reasonable for purposes of this application.

B. *Rate Structure*

The Authority increasingly is recognizing the necessity and merit of cost of service studies in determining fair and reasonable utility rates, especially amongst the larger utilities within its jurisdiction. In this respect we are of the

opinion that such companies should present a complete, detailed and impartial cost of service study in support of requested rate increases. In the instant case, the Company has presented an incomplete study in order to expedite the timing of the hearing, although we had fully expected submission of a more complete and detailed study as part of the Company's presentation. We are disappointed that the study did not present a more in-depth analysis, especially of the reasonableness of the existing six-block rate structure. Although the Company's witness felt this structure to be appropriate, we are aware of current industry practice to simplify the declining block structure to a minimum block and perhaps two subsequent blocks appropriately designed to recover the revenue requirement from each class of customer.

The study presented by the Company indicated that the Metered Residential class is producing less revenue (as a percent of total revenue) than deemed proper by the study (see Reinert Exhibit No. 7); and, conversely, the Flat Rate class is producing more revenue than required. The Company, therefore, proposes to increase the minimum meter charge (and, therefore, the entire metered category) by a higher percentage (22.3%) than the Flat Rate category (15.0%). Inasmuch as the revenue requirement has been allocated on the basis of relative total water usage and peak hour demand between these two classes, we question the validity of the Company's study in this respect. We fail to see, and certainly are far from convinced by the Company's explanation of its cost of service study methodology (see Exhibit 36), that water usage can accurately be attributed to an unmetered user. Indeed by arbitrarily increasing or decreasing the amount of unaccounted for water, the amount "left over" and attributed to flat rate users can be correspondingly decreased or increased. We therefore, see little basis for allowing the differential increases as proposed by the Company between the Flat Rate and Metered categories.

Based on the above, we are of the opinion that the Company should submit as part of its next rate case filing a complete, detailed cost of service study performed independently by a qualified consultant. In addition to addressing proper allocation of revenue requirements to general water service and fire protection service, the study should further suballocate the revenue requirement between the various metered, flat rate and fire protection classes. Ogive curves developed from an appropriate bill analysis, should be presented along with an evaluation of alternative, more simplified rate structures.

Accordingly, lacking a detailed and complete cost of service study in the instant case, we shall direct that the increased revenues granted hereinafter be allocated uniformly to all classes of customers.

C. *Revenue and Revenue Adjustments*

According to the Company's Exhibit No. 6, actual test year revenue was shown as $16,388,372. Adjustments to test year revenue were indicated in the amount of $64,390 resulting in pro forma revenue at present rates of $16,452,762. As required by the Authority, the Company prior to the hearing submitted a revised revenue Exhibit No. 6 detailing the adjustments to test year revenues by class of customer in arriving at the pro forma at present rates column. The Authority's review of each adjustment as further detailed on the Company's exhibit, especially in the adjustments shown for the Flat Rate, Metered Residential, Commercial and Industrial classes indicated some discrepancies as compared with previously submitted annualization data. For purposes of the instant case we shall accept the pro forma revenue amounts at present rates as indicated on this exhibit with the exception that we shall allow a decrease of $15,200 at present rates and $17,000 at proposed rates to reflect the loss of an industrial customer (see Late File Exhibit No. 81). However, we shall expect in future filings that the "Adjustment" column to Test Year revenues, for each class of customer, be fully and accurately detailed, supported by separate annualization, billing or other adjustments.

In the Flat Rate category, we note that the Company's estimate of pro forma revenue at present rates is based on the number of flat rate customers as of December 31, 1976. In our opinion, and as acknowledged by the Company's witness, the actual number of flat rate customers, pro forma, will be substantially reduced as a result of the on-going meter conversion program. According to the Company's Late File Exhibit No. 54, the flat rate revenue pro forma at present rates should properly be reduced by $128,602. Since the Company's studies indicate that approximately the same revenue is derived on a metered basis from a former flat rate user, we shall increase pro forma revenue at present rates in the Metered Residential category by the same amount, $128,602. Although the net effect of these two adjustments is zero, the Company in computing the amount of increased revenue by class as granted hereinafter shall revise its Exhibit No. 6 figures pro forma at present rates, accordingly.

Concerning the Company's bill analysis submission, Exhibit No. 42, we note that this is characterized as an "Annualized" bill analysis. The former PUC, in Docket No. 11736, dated November 25, 1975, directed the Company (see specifically Page 16, Condition B.2.) to ... "make all necessary changes to its data processing program so that in future rate cases, a true bill analysis reflecting *actual test year consumption* will be present" (emphasis added). The Company contended that, although its bill analysis and bill analysis summary sheet reflect internally computerized annualization of new customer accounts, and an analysis of actual test year consumption is done internally by its computer, the printout of same would be extremely voluminous. The Authority is aware that there are costs associated with performing such analysis. However, we are striving to standardize the bill analysis submissions which are routinely submitted as part of the rate case procedure by the various larger, metered water utilities under our jurisdiction. We, therefore, shall direct that the Company submit to the Authority a cost estimate related to the re-

programming and/or other changes needed such that the bill analysis printout will reflect actual (and not annualized) test year consumption experience.

The adjustments to the Company's pro forma revenues to reflect the loss of a large industrial user as noted above are shown in Table II below.

D. *Construction Program*

The Company's presentation projects its total construction expenditures through 1981, the bulk of which relate to complying with the new quality standards which became effective June 1, 1977. The Company's projected demands show little growth. No increase in sources of supply is contemplated in the next five years, and only limited additions in ten years.

Upon all the proof, the Authority accepts the proposed construction program for the years 1977 - 1981, for the purposes of this proceeding.

The Company shall continue, in all future related submissions, to calculate its safe yield determination on a 95% dry year basis as ordered by the Authority in Docket No. 11639.

E. *Depreciation*

The selection of appropriate rates of depreciation is dependent upon informed judgment, experience and knowledge of the industry under review with particular emphasis on the company in question. The Authority's analysis of the Company's proposed depreciation rates indicates no significant differences between the rates now employed by the Company and those proposed by its witness. As noted above, at December 31, 1975 the Company's rates produced an overall composite figure of 1.76% while use of the proposed rates resulted in a composite rate of 1.78% (Ex. 58, Schedule 1). Applied to plant balances as of December 31, 1976, the Authority calculates that the composite rates became 1.81% and 1.82% respectively. Upon consideration of all pertinent data we conclude the depreciation rates now used by the Company reasonably measure the depreciation

accruing on its water plant in service and we are not persuaded that any change in rates should be made at this time.

The Company's position that there is a new dimension to depreciation, namely, a financial aspect is inopposite. The annual depreciation expense recorded on a utility's books is set therein for the recoupment of the original dollars of investment in the property being depreciated (loss in service value) in the service of its customers and for no other purpose. There are other avenues along which to proceed towards the solution to the problems of financing the replacement of present plant with the more costly dollars of today and tomorrow, discussed further on in this decision.

F. *Rate Base — Table I*

The $61,376,000 rate base originally claimed by the Company consists of the depreciated cost of actual plant in service at December 31, 1976, plus construction work in progress of $324,000 representing costs incurred in the test year relating to the construction of the Trap Falls filter plant and an estimated $1,027,000 representing the cost of plant to be in service by, or in close proximity to, the hearing date. The said rate base also includes an allowance for working capital and supplies and a reduction for customer advances and contributions.

During the hearing, the Company presented an exhibit which purported to show the cost of actual utility plant additions during the period January thru April, 1977 amounting to $883,967 net after deducting customer advances. The Company requested that the said $883,967 be added to its rate base in lieu of the $1,027,000 originally proposed since it represented known utility plant cost additions which occurred subsequent to the end of the test year.

In our analysis of the $883,967 cost we are of the opinion that there is no single project in it with a cost of such magnitude as to warrant special consideration by the Authority. It is the Authority's position that a rate base should

not include the cost of plant which is not rendering service to customers at the end of a test year, except for known changes of individual items of some magnitude. Since the Company did not offer a revised rate base exhibit which would reflect the change in the cost of plant beyond the test year the Authority makes its adjustments to the rate base as originally proposed by the Company and therefore excludes the amount of $1,027,000 for purposes of this rate application. The Authority holds that depreciation rates now used produce a composite of 1.82 resulting in an adjustment of the Company's pro forma depreciation expense of $51,000. The related adjustment is also reflected in the Reserve for Depreciation Account.

The Authority also disallows the proposed inclusion in the rate base of $324,000 representing construction work in progress related to the Trap Falls filter plant. Our reasons for the disallowance is explained in Section H of the Authority's Analysis.

We show in Table I, below, the rate base claimed by the Company and adjusted by the Authority for purposes of this rate application.

TABLE I

	Company Pro Forma	Authority Adjustment	Authority Allowed
Utility Plant	$96,218,000	$(1,027,000)	$95,191,000
Less: Work in Progress	378,000	(324,000)	702,000
Held for Future Use	254,000	—	254,000
Reserve for Depreciation	26,463,000	51,000	26,412,000
Net Utility Plant	$69,123,000	$(1,300,000)	$67,823,000
Add: Working Capital	718,000	—	718,000
Materials and Supplies	497,000	—	497,000
Total	$70,338,000	$(1,300,000)	$69,038,000
Less: Customer Advances	5,252,000	—	5,252,000
Customer Contributions	3,710,000	—	3,710,000
Rate Base	$61,376,000	$(1,300,000)	$60,076,000

G. *Financial Data*

1. *Cost of Money — Rate of Return — Attrition Allowance*

Mr. Joseph F. Brennan, President of Associated Utilities Services, Inc., of Cherry Hill, New Jersey was the applicant's witness in the areas of cost of money, rate of return and attrition analysis. Mr. Brennan concluded in a recommended rate of return of 9.75%, inclusive of a provision for attrition and lag of .26%, which he admitted was rounded to arrive at an even quarter percent was an appropriate rate of return.

If no CWIP were to be allowed in the rate base, and therefore no short term debt included in the capital structure, the implicit recommended rate of return by Mr. Brennan is as follows:

Capital	Ratios	Cost Rate	Weighted Cost
Debt	52%	6.03%	3.14%
Preferred	12	10.47	1.26
Common	36	14.90	5.36
Bare Cost			9.76
Provision for Attrition and Lag			.24
Rate of Return			10.00%

Intervenors also introduced testimony through Edgar H. Bernstein, a consultant, and President of Associated Regulatory Consultants, Inc., of Washington, D.C. to the effect that CWIP should be disallowed in rate base. This is discussed more fully in another part of this decision analysis.

Mr. Brennan stated in his cross-examination that his recommended rate of return of 9.49% also incorporated in its before-income-tax interest test the advantages of complete normalization of all time differences for accounting and rate purposed as filed by the Company. He claimed this because he used an effective tax rate of 32.2%, taken from the Company accounting exhibit.

In arriving at the 14.5% recommended return on equity, Mr. Brennan utilized a considerable bank of data.

Our review of the data and the testimony of Mr. Brennan does not show a clear bridging of the gap between the raw data and the conclusion of 14.5% as reached by Mr. Brennan. We agree that informed judgement is one ingredient in the overall assessment of an allowed return on equity, but the raw data in this case do not come close enough to Mr. Brennan's conclusion to explain the gap by simply "informed judgement". It could be argued that the 7 Barometer Water Companies show a 1976 trended 14.5% E/P ratio, but Mr. Brennan did not rely solely upon that approach, and the trending was done by the Authority staff in that instance, and not by Mr. Brennan. When asked (TR 12) if the subsidiary were actually getting common equity (from the 1977 sale) from the parent at a lesser cost than the parent got it from the market, Mr. Brennan replied, "That's correct".

Mr. Brennan also employed several analytical tools to reinforce his judgment, such as general economic developments, which were subject to some extent to his own interpretation. He used the bare rent theory (with its own assumptions) and industrial (non-regulated) comparisons as a check rather than primary evidence.

The primary thrust of Mr. Brennan's testimony, however, revolves around the question of interest coverage and coverage of fixed charges. Mr. Brennan believes the Hydraulic Company (specifically Bridgeport Hydraulic Company) should maintain a financial profile (presumably through regulation) comparable to that of an AA Standard & Poor's rated, or Aa Moody's rates utility.

On cross-examination Mr. Brennan admitted that neither The Hydraulic Company nor Bridgeport Hydraulic Company now enjoyed such creditability (none of its bonds or preferred stock are rated). Historical

coverage levels and costs of issuance related to the market at the time of issuance indeed indicate that Bridgeport Hydraulic has maintained a financial profile barely equivalent to that of an A rated utility (Schedule 9, of Exhibit B 1).

Bridgeport Hydraulic Company now has an embedded long-term debt cost of 6.03% and total debt cost of 6.12%, accepting Mr. Brennan's estimated 7.5% short-term debt cost rate. Its combined prospective embedded senior capital cost (debt and preferred), inclusive of short-term debt, is 6.91%, and excluding short-term debt it is 6.88%. Bridgeport Hydraulic Company will not have to face a major debt refunding until November of 1980, at which time about $6 million of 3% money will have to be replaced by probably more costly capital. That refunding is not a consideration for this proceeding, since the Company will have ample time to file a subsequent aplication for rate relief prior to the time of its 1980 refunding if relief is necessary at that time.

With regard to Mr. Brennan's study, concerning the cost of common equity varying by .2-.3% with each 1% change in the common equity ratio, we do not believe the evidence in this case is conclusive. The evidence presented was in the form of an analysis of AT & T, as previously mentioned, and in our opinion is inconclusive in that it involves one system, rated AAA with regard to its unsecured debt, with vastly different overall risk characteristics from a water utility and it covers a period of time during which other economic phenomena may or may not have contributed to such variation in return levels.

In our opinion, an approximate 6% embedded long-term debt cost and a return of 13.2% on common equity of $22,435,000 (representing common equity of $19,235-000 at the end of the test year plus $3.2 million donated to the Company as additional paid-in capital resulting from the sale of 200,000 shares of common stock

through the parent, (The Hydraulic Company) should be adequate to enable Bridgeport Hydraulic Company to continue to attract capital on at least as favorable terms (basically an A+ – rated profile) as it has in the past, and probably slightly more favorable terms in the period of prospective rate making. The Company has taken initiative in fortifying its common equity ratio with its recent (indirect) sale of common stock. At this time, an AA credit profile is not indicated, nor is it necessary, in our opinion, in order to comply with the standards of capital attraction, credit level maintenance and comparable risk returns set forth in the Hope and Bluefield cases before the U.S. Supreme Court. Therefore, we conclude that a reasonable allowance for the return on common equity in this case in 13.2%. This is based upon a complete consideration and weighing of the evidence presented before this Authority, and upon our opinion that at this time attainable interest and fixed charge coverages for Bridgeport Hydraulic are adequate.

Based upon a careful review, consideration and weighing of all evidence presented in this case, it is the Authority's conclusion that the fair rate of return should be based upon the 1976 calendar year with adjustment for known changes of items of some magnitude (i.e., the cost of recently sold common equity).

Since the Company made no showing of continued attrition in the future, by introducing a forecast, budget or trend of operating expenses, rate base increases and revenues, fully adjusted, we can provide no prospective attrition allowance in this case.

The fair rate of return to be applied to the allowed rate base of Bridgeport Hydraulic Company in this case, is therefore 9.5%.

We believe that we are obliged to give due consideration to the interests of the consumers, as well as the interests of the investors, in determining revenue requirements. Ac-

cordingly, the Authority has found that the revenue herein provided should be sufficient not only to cover operating expenses, but also to generate funds for plant improvement and internal working capital. These conclusions are reached after a careful review of all the evidence and testimony including, but not limited to, the Company's construction program, its capital structure, and an appropriate level of earnings.

2. *Normalization vs. Flow Through of Income Taxes and Service Life Method vs. Initial Year Flow Through of Job Development Credit*

Mr. Jay H. Price, Partner of Arthur Anderson & Co., of Chicago, Illinois, the applicant's witness recommended that tax depreciation should be normalized both for accounting and rate purposes. He also concluded that not to do so would involve a higher cost of capital, and would fail to recognize the "cost" of using up available tax deductions. Finally, with regard to the investment tax credit and job development credit, Mr. Price concluded that they were not timing differences as such, but rather they were permanent tax savings, and should be treated by normalization and the service life method respectively.

Mr. Price claimed that when the predecessor commission to this Authority reached its initial decision in flow-through accounting about 20 years ago, it did not have available many of the accounting "factors" and economic "effects" of normalization and flow through it now has.

Under cross examination Mr. Price admitted that the present Authority did in fact have at its disposal all such information when it reaffirmed its position on normalization at the 1975 Generic hearing. He himself was a witness in that proceeding. It was also brought out on cross examination that Mr. Price has not made a first-hand study as a financial expert of the investor assessments of such treatment as normalization vs. flow

through. He had made no quantifiable study to demonstrate this point, but ruled solely upon hearsay testimony of others not present for cross examination.

Mr. Price claimed that another cost of accelerated depreciation is involved — that of using up a tax deduction. This brings us to the benefit of normalization. If there is a benefit of normalization to the Company, there is an equal and corresponding detriment to the customer, in terms of lost present value and the purchasing power dollar alternatives. Mr. Price states that the real value of normalization to a utility is the time value of money. When Mr. Price was pressed concerning a second possible benefit (in inflation) of the presence of dollars having higher purchasing power, he admitted that this too could be. The real benefit of normalization to the Company is based upon a continuation of inflation. It also must be born in mind that normalization adds to inflation rather than helps abate it. Correspondingly, the equal and opposite force is felt by the consumer, who also needs his dollars today, when his or her purchasing power is higher.

Obviously, with normalization today's consumer bears the brunt of the cost for tomorrow's rate payer. Since we are anticipating inflation, the dollars of cost today are more costly (in purchasing power) than those which will be spent tomorrow, and the entire procedure becomes more costly to the consumer.

Many of Mr. Price's exhibits are based upon an assumption that is unproven in the record — namely that if normalization exists in a cost atmosphere of 11% rate of return, flow-through will exist in a cost atmosphere of 11.5%. There simply is no expert evidence one way or the other to demonstrate the accuracy of this assumption.

We have dealt at length with this entire question, generically in 1975, and find no reason to change our view. It may well be that we are in the minority of states in requiring continued flow-through treatment

but we do not regard that as reason to change our position at this time.

Therefore, we continue for the present, at least, to reject normalization of taxes for timing differences, for reasons we have stated.

Based upon a careful review, consideration and weighing of all evidence presented in this case, it is the Authority's conclusion that present flow-through treatment of all timing differences resulting from accelerated depreciation be continued for both accounting and rate purposes.

H. *Construction Work in Progress*

Traditionally, construction work in progress has not been included in the rate base of regulated public service companies in Connecticut. Currently, the Company capitalizes, as part of an asset's total cost, an allowance for funds used during construction (AFUDC).

The Authority is aware of Bridgeport Hydraulic's construction program which to a large degree is needed in order for the Company to comply with federal and state water quality standards. The Authority is also aware of the Company's need to raise large amounts of capital to finance its construction program. However, before the Authority is willing to deviate from its past policy on the treatment of construction work in progress in an individual rate case, the Authority desires to have the benefit of a generic hearing on the appropriateness of permitting construction work in progress in the rate base of water companies which are required to comply with The Safe Drinking Water Act.

Any decision arrived at in this rate case would have significant implications and would establish a precedent for any and all future applications. The better course would be for the Authority to decide on the merits of including or excluding construction work in progress in the context of a generic hearing where all interested persons could contribute to the Authority's consideration of the issue.

For the reasons herein stated, the Authority has decided, for the time being, to continue its historic treatment of

construction work in progress and has decided not to include CWIP in Bridgeport Hydraulic's rate base.

I. *Expenses*

Subsequent to the filing of the original application, the Company deemed it necessary to adjust by additional exhibits certain of its proposed expenses for pro forma purposes from those originally filed in order to reflect known changes which had been incurred by the Company since the original filing of the application. The additional expenses are as follows:

Operation and Maintenance Expenses	$81,000
Property Taxes	35,000

Since the Company did not submit a revised pro forma Income Statement to reflect the known changes, they are, for purposes of this application, reflected in the "Authority Adjustment" column of Table II.

The pro forma expenses claimed by the Company are acceptable for determining the Company's revenue requirements at this time, with the following exceptions.

The Company has, as evidenced by an exhibit, experienced since 1972 gains from the sale of property the cost of which was originally part of its rate base. The net gains reported "above-the-line" and resulting in a reduction of operating expenses as required under the Uniform System of Accounts prescribed for water companies were as follows:

1972	$ 64,000
1973	111,000
1974	276,000
1975	19,000
1976 (test year)	144,000

For pro forma purposes the Company eliminated the net gain of $144,000 experienced in the test year from the sale of land whose cost was originally recorded as plant in service on the grounds that "profits from the disposition of land should not be considered in the rate-making process". Upon cross-examination, the Company witness stated that land

not necessary in the water operation would continue to be available for sale as far as the Company was concerned. As a matter of fact, the Company's President and Chief Executive Officer made the statement before a recent meeting with a legislative committee that the Company planned to sell 200 acres of its surplus land each year for the next five years. The witness further stated upon cross examination that profits from land sales were not considered non-recurring but that they should be considered "below-the-line" so that they are not considered in the rate-making process. He would not agree that, in view of the Company's intention to continue selling its excess land, an average of the five-year profits should be considered as an "above-the-line" item and reasonable for pro forma purposes. The Authority does not agree with the witness's contention that the profits from land sales should not be reflected "above-the-line" for rate purposes. We are of the opinion that so long as the present accounting regulations are in effect regarding the treatment of profits from land sales, the regulations must be conformed with by the Company for book and rate purposes. Since the record shows, and it was testified that, the sales of lands appear to be an on-going type of transaction, some benefit from those sales should inure to the ratepayer in a rate application. We, therefore, are of the opinion that a 5-year average of the pre-tax net gains, or $123,000 from the disposition of land whose cost was at one time a part of the Company's rate base is proper and reasonable to be included in the Company's income statement for pro forma purposes. Our calculation of the pro forma federal income and Connecticut business taxes reflects a capital gains tax on the said net gain of $123,000.

The account, Outside Services Employed, reflected Company legal and other expenses of $284,000 incurred in the test year. For pro forma purposes the Company proposes to reduce the expenses by approximately $192,247 for those charges which are considered non-recurring. Legal expenses incurred and charged to the account since 1971 were shown in a requested late-filed exhibit as follows:

1971	$ 25,000
1972	8,000
1973	17,000
1974	21,000
1975	104,000
1976 (test year)	238,000

The Company claims that the large legal expenses incurred in 1975 and the test year resulted principally from the fact that the Company's in-house counsel resigned in mid-1975, causing the Company to seek outside legal assistance since that time. We are aware that the Company has, in the past few years, been a party to various out-of-the-ordinary legal proceedings thereby resulting in larger than normal legal costs being incurred. The Company witness at cross examination was of the opinion that these higher than normal legal expenses will continue to be incurred for some time in the future, but did not offer any concrete evidence to convince the Authority that his opinion was based on facts. We decrease the Company's request of $91,753 ($284,000 less $192,247) to $78,000, the average of the 1972-76 charges, as an amount being more representative of legal and other charges to be incurred for pro forma purposes, and therefore reduce operating expenses for purposes of this application by $13,753.

The Company proposes source of supply expenses of $156,948, the amount incurred in the test year in Account No. 603, Miscellaneous Expenses. Test year charges to this account include approximately $6,700 incurred in the latter part of the year for services performed on behalf of the Company by an outside firm in preparing to testify before the State Health Department and the Council on Water Company Lands. At the hearing the Authority staff questioned why these expenditures should be considered recurring in nature. A requested late-filed exhibit which was to support the Company's contention that the charges were indeed recurring in nature indicated that the Company "considered this type of work to be recurring". Further evidence submitted was to the effect that, because of the

concern on the part of the Company over the Council's proposals as they relate to land policies, the Company expected this type of expenditure to continue in the future. The Authority believes that the amount of $6,700 should not be allowed for pro forma purposes because the Company has not carried the burden of proof as to reasonableness of the charge. It is therefore disallowed by the Authority.

Current rate case expense is estimated to total $50,000 which the Company proposes be amortized over two years. The expense includes $15,000 representing the cost of management services performed by The Hydraulic Company officers in the preparation of this rate case. At the hearing and as a result of cross examination, the witness stated that the charge was a duplication of another adjustment and therefore should be eliminated from the rate case expense. The Authority for pro forma purposes reduces the Company proposed rate case expense by one-half of the $15,000 or $7,500.

Pro forma taxes charged to operations amount to $2,605,000 were originally proposed by the Company in the application. Subsequent to the original filing, the Company amended its proposal to increase the pro forma amount by a net of $35,000 to reflect certain changes which had occurred in mill rates and assessments not known at the time of the original filing. The pro forma amount of $2,640,000 as finally adjusted by the Company included property taxes of $38,730 and $883,967 of utility plant not allowed by the Authority to be included in the rate base as hereinbefore detailed. Since the cost of the utility plant is not allowed, the related property taxes are also disallowed by the Authority.

Management charges of $387,711 are proposed by the Company for pro forma purposes. These charges include certain allocable expenses incurred by The Hydraulic Company, (the parent) such as fringes, officers' expense, outside services, stockholder's expense, directors fees, etc. In addition, the management charges include The Hydraulic Company officer salaries directly allocable to the Company.

An exhibit indicated that total management charges amounted to approximately $327,000 in 1975 and $339,000 in the test year. The proposed pro forma management charges represent an approximate increase of 14% over the test year and an 18% increase over the year 1975. *The Authority is of the opinion that since the review of the in-depth management audit, which will specifically address the reasonableness and allocation of these salaries, is incomplete it is impossible to determine the reasonableness of the charges.* The $339,000 incurred in the test year by the Company appears to be the proper amount to be charged the ratepayers for the purposes of this rate application. We are cognizant of the fact that costs have increased and that under the consolidated arrangement (parent-company relationship) certain costs incurred by the parent must be passed on to the operating company; however, we are also cognizant of the fact that under a consolidated arrangement certain savings are supposed to occur which would not otherwise be experienced by the operating company. Even though the Company is convinced that savings in fact have occurred from the consolidation, we are not equally so convinced. The Authority therefore reduces the Company's requested $387,711 charge by $48,711 for purposes of this application until such time as the management audit is complete and further review of the reasonableness of the charges can be made by the Authority.

In reporting and allocating officers' salaries, the method used to report and allocate Mr. Silliman's salary had been changed between 1975 and 1976. No Company witness was able to explain to the satisfaction of the Authority why Mr. Silliman's salary should be allocated any differently than that of other officers. *For the purpose of future rate cases, Bridgeport Hydraulic is ordered to employ the same method in reporting and allocating Mr. Silliman's salary as is used to report and allocate all other officers.*

For pro forma purposes the Company, although opposing the method, calculated a federal tax liability and reflected it in its Income Statement in accordance with the method

prescribed by this Authority and detailed in recent rate applications of sister companies (Docket No. 760702 dated December 13, 1976, Norfolk Water Company; Docket No. 761107 dated April 19, 1977, North Canaan Water Company; Docket No. 760701 dated January 3, 1977, Litchfield Water Company), who participate as members of a holding company system in the filing of a consolidated federal income tax return. An exhibit indicated that an effective tax rate of 33.7%, the average of the years 1971 - 1975 effective tax rates (with the 1975 actual consolidated tax liability adjusted upward to reflect the election of the normalization on the additional 6% Investment Tax Credit for accounting and rate making purposes as required by the Tax Reduction Act of 1975) was utilized in determining the Company's share of the pro forma tax liability. Since the year 1975 is the most current year of available data in order to calculate the effective tax rate on an average five-year basis, the Authority is of the opinion that for pro forma purposes the 33.7% effective tax rate as developed should be utilized in computing the Company's tax liability for purposes of this rate application as a reasonable approximation of a future effective tax rate.

The Authority calculates that at the proposed rates requested and after adjustments to revenues and expenses as detailed above, and utilizing the effective tax rate of 33.7%, the Company's federal tax liability on a consolidated basis would be $1,472,321 or $472,679 less than that proposed by the Company.

In the same vein, the Company has computed for pro forma purposes the Connecticut State Business tax by utilizing an effective tax rate of 8.7% based on an average of the three-year historical effective tax rates experienced in the years 1973 - 1975 from filing a combined or consolidated return with the 1973 and 1974 actual tax liabilities adjusted to reflect the 1975 increase in the statutory rate from 8% to 10%. This method of calculating the effective tax rate for pro forma purposes is in accord with that used by the Authority as detailed in the recent rate applications of the

sister companies referred to above. Since the experience through 1975 is the most recent data available to the Authority, we will consider the said 8.7% effective tax rate as a reasonable approximation of expected future operations. By applying it to the taxable income, as adjusted by us for pro forma purposes, we calculate the Connecticut State Business tax to be $418,508 or $41,492 less than that proposed by the Company.

While the Authority has approved the Company's employee wage adjustment, the Authority is very much concerned with what appears to be a Company compensation policy aimed at maintaining a position of leadership in the community. The policy appears to have resulted in average compensation rates increasing more rapidly than the consumer price index, without parallel increases in productivity. This seems to be inappropriate for a regulated public service company in that it requires the ratepayer to provide company employees with a greater degree of protection against inflation than they themselves enjoy in an inflationary economy. A more appropriate posture would seem to be one aimed at insuring that the Company's employees fare no worse in the face of inflation than the labor market from which the company's employees are drawn (this is a far more appropriate standard of comparison than other utility companies since as a general rule BHC is not competing with other utilities for labor but is competing with all other employers within the Bridgeport area).

In the future the Authority will accept for ratemaking purposes those wage and salary adjustments designed to maintain parity within the labor market involved and will not accept settlements in excess of this norm without specific evidence as to the need and necessity for such increases.

J. *Summary*

Table II, below, shows the pro forma income statement at the proposed rates as presented by the Company, the adjustments made by the Authority and the pro forma as modified by the Authority:

TABLE II

	Company Pro Forma at Proposed Rate	Authority Adjustment	Company Pro Forma With Authority Adjustment
Operating Revenues:			
Present Rates	$16,453,000	$(15,200)	$16,437,800
Proposed Increase	2,841,000	(605,800)	2,235,200
Total Operating Revenues	$19,294,000	$(621,000)	$18,673,000
Operating Expenses:			
Operation and Maintenance	$ 5,742,000	$ 4,336	$ 5,746,336
Gain on Sale of Property	—	(123,000)	(123,000)
Depreciation	1,586,000	(51,000)	1,535,000
Taxes —			
Property	2,605,000	(3,730)	2,601,270
Gross Earnings	973,000	(31,050)	941,950
Connecticut Business	460,000	(41,492)	418,508
Federal Income	1,945,000	(472,679)	1,472,321
Total Operating Expenses	$13,311,000	$(718,615)	$12,592,385
Utility Operating Income	$ 5,983,000	$ 97,615	$ 6,080,615
Other Income	4,000	—	4,000
Total Income	$ 5,987,000	$ 97,615	$ 6,084,615
Interest Expense	1,940,000	—	1,940,000
Net Income	$ 4,047,000	$ 97,615	$ 4,144,615
Preferred Dividends	809,000	—	809,000
Income Available for Common	$ 3,238,000	$ 97,615	$ 3,335,615
Rate of Return	9.75%		10.12%

The Authority analysis indicates that the Company's rate of return at the present rates is less than just and reasonable, and that the Company is in need of additional revenues if it is to continue to provide adequate and efficient service in its franchise area. The analysis of the evidence presented also indicates that the return the Company would receive at the proposed rates after payment of its operating expenses, depreciation and taxes on the rate base as adjusted by the Authority would be 10.12%, which is more than just and reasonable and would provide an operating income in excess of that which is necessary in order to enable the Company to maintain its financial stability, to provide adequate service and to afford it a reasonable return.

K. *Analysis of Intervenor's Positions*

The issues addressed by the Office of Consumer Counsel have been dealt with at length in other sections of this decision. See Section IV., E., F., 2, H., and I. The Authority has considered the evidence and arguments offered by the Consumer Counsel in its analysis and evaluation. The Authority is appreciative of the Consumer Counsel's contribution in this rate case and has incorporated his suggestions where considered proper.

The Authority is sympathetic to most of the concerns expressed by various towns, persons and groups which appeared before the Authority. The Authority has considered the various intervenor's positions in arriving at its decision. Given the state of the economy, the Authority is aware of the plight of the residential consumers, elderly consumers living on fixed incomes and municipalities in meeting increased utility expenses. The Authority makes this decision and all of its decisions in accordance with specific guidelines and principles established by statute. In part, Connecticut General Statute, Section 16-19e provides that ". . . the Authority shall examine and regulate . . . the establishment of the level and structure of rates in accordance with the following principles: . . . (4) that the level and structure of rates be sufficient, but no more than sufficient, to allow public service companies to cover their operating and capital costs, to attract needed capital and to maintain their financial integrity, and yet provide appropriate protection to the relevant public interests, both existing and foreseeable; and (5) that the level and structure of rates charged customers shall reflect prudent and efficient management of the franchise operation".

V. FINDINGS OF FACT

A. *Authority Allowed — Table III*

1. The test year for this rate application is the operating and revenue experience of the Company for the twelve months ending December 31, 1976, which we

find is reasonable as a basis for the Company's application and is hereby accepted.

2. The appropriate rate base for this rate application is $60,076,000.

3. The Company's rate of return at the present rates is less than just, reasonable and adequate to allow the Company to fulfill its statutory duty to the public.

4. In consideration of the adjustments made by the Authority as detailed hereinbefore, the full increase sought by the applicant in the proposed amendment to the existing schedule of rates on file is denied.

5. The Authority finds than an allowance of additional revenues amounting to $1,585,885 will provide the Company with utility operating income of $5,707,220.

6. The operating income of $5,707,220 will allow the Company a rate of return of 9.5% on the rate base as adjusted by the Authority and a return on common equity of 13.20%.

7. The Authority finds that a rate of return of 9.5% represents the minimum necessary to enable the Company to attract capital at reasonable costs, to assure continued, adequate and safe service and to provide for necessary expansion to meet future requirements.

8. Table III, below, shows the revenues and expenses found reasonable by the Authority:

TABLE III

Operating Revenues:	
Present Rates	$16,437,800
Allowed Increase	1,585,885
Total Operating Revenues	$18,023,685
Operating Expenses:	
Operation and Maintenance	$ 5,746,336
Gain on Sale of Property	(123,000)
Depreciation	1,535,000

Taxes —	
Property	2,601,270
Gross Earnings	909,487
Connecticut Business	364,842
Federal Income	1,282,530
Total Operating Expenses	$12,316,465
Utility Operating Income	5,707,220
Other Income	4,000
Total Income	$ 5,711,220
Interest Expense	1,940,000
Net Income	$ 3,771,220
Preferred Dividends	809,000
Income Available for Common	$ 2,962,220

9. Rates and revenues at this level are not unreasonably discriminatory or more or less than just, reasonable and adequate to enable the Company to provide properly for the public convenience, necessity and welfare.

VI. DECISION

Based on the foregoing, the amended schedule of rates as filed with the Authority is denied. Additional revenues in the approximate amount of $1,585,885 over the annual revenues received by the Company under its present rates is approved subject to the following conditions:

1. The applicant shall file a schedule of rates designed to produce the revenues granted herein and when approved by this Commission shall become effective five (5) days after approval for service rendered on and after said effective date, except public fire protection service which shall become effective as provided in Section 16-19 of the Connecticut General Statutes. The increase in rates shall apply uniformly to all classes of customers.
2. Conditional to its next rate case filing, the Company

shall submit a complete, detailed cost-of-service study performed by a qualified, outside consulting firm. In addition to properly allocating expenses among the various classes of customers, the study shall place particular emphasis on the reasonableness of the existing 6-block rate structure and include an analysis of alternate, and simpler rate structures.

3. Within 90 days, the Company shall submit detailed data concerning the nature and related costs of any changes required in the existing bill analysis computer program such that the bill analysis printout shall reflect actual (unannualized) test year consumption data.
4. For the purpose of future rate cases the Company is to report and allocate the salary of Mr. Silliman in the same manner as is used to report and allocate the salaries of other Company officers.

We hereby direct that notice of the foregoing be given by the Executive Secretary of this Authority by forwarding true and correct copies of this Decision, to parties in interest, and due return make.

Dated at Hartford, this 30th day of June, 1977.

Miriam B. Butterworth
Gerald J. McCann
Richard O. Jones
} PUBLIC UTILITIES CONTROL AUTHORITY

State of Connecticut
County of Hartford
} ss. Hartford, June 30, 1977

I hereby certify that the foregoing is a true and correct copy of Decision issued by the Public Utilities Control Authority.

Attest: Henry Mierzwa

Executive Secretary, Public Utilities Control Authority

See Following Page for Concurring Opinions of Commissioners Richard O. Jones and Miriam B. Butterworth.

Concurring Opinion — Docket Number 770301

I am concurring in this decision and in the rate of return agreed upon by the other two commissioners assigned to this panel. In my judgment the amount of increase granted is appropriate under all the circumstances.

However, *I believe that the following matters should be further investigated in an expanded managerial audit: the entire corporate structure, the amounts of some of the corporate salaries, the methods of allocation of those salaries, and the expense accounts of some of the officers of the company.*

Although most of these items that have a monetary value do not amount to a significant percentage of the Company's expenses, nevertheless, they may not conform to the most desirable managerial principles that a regulated company should follow.

In addition any significant transactions between Bridgeport Hydraulic Company and the Silliman Company in which Mr. Silliman owns a controlling interest, should be thoroughly explored.

I shall therefore suggest that the managerial audit now being performed be expanded to focus on the above matters.

Miriam B. Butterworth
Vice Chairperson

Concurring Opinion — Docket Number 770301

In the instant case the panel elected to defer a decision with respect to the company's request to include construction work in progress in the rate base, pending the outcome of a generic hearing ordered by the Authority on that subject. While I understand the precedential impact that a decision in the instant case cold have had on other matters currently pending before the Authority, I believe that the question of CWIP could have been dealt with within the present framework. Since the impact of excluding CWIP is not extreme in the first year and since, presumably, the company will be able to conform with the decision in the

generic proceeding as soon as it is rendered, I do not consider this flaw to be fatal and hence I do not dissent.

I do want to make the following statement, however, with respect to the inclusion of CWIP in the rate base as it pertains to the construction necessary to conform with the provisions of the Safe Drinking Water Act. The circumstances surrounding this issue, for the most part, are unique. The requirements of the act were imposed by the Federal and State governments and are totally beyond the control and discretion of the company. These investments will result in no increased revenues and their impact on rates may result in decreased consumption of water. The magnitude of the expenditure is very dramatic in relation to total investment in company plant. In the case of Bridgeport Hydraulic, the cost of the Trap Falls filter plant is estimated to be some $14 million which equals 23.3% of the company's rate base. The need to finance such sums is clear and the ability to do so is suspect without the assurance of a return on that investment.

In summary the problem is sufficiently unique to require a unique solution, which in my opinion can only be the inclusion of CWIP on a selected basis in the company's rate base.

Richard O. Jones
Commissioner

Relevant Portions of the Uniform System of Accounts Prescribed for Water Utilities

UTILITY PLANT INSTRUCTIONS

* * * *

7. Land and Land Rights.

A. The accounts for land and land rights include the cost of land owned in fee by the utility and rights, interests, and privileges held by the utility in land owned by others, such as leaseholds, easements, water and water power rights, diversion rights, submersion rights, rights of way, and other like interests in land.

B. Where special assessments for public improvements provide for deferred payments, the full amount of the assessments shall be charged to the appropriate land account and the unpaid balance shall be carried in an appropriate liability account. Interest on unpaid balances shall be charged to the appropriate interest account. If any part of the cost of public improvements is included in the general tax levy, the amount thereof shall be charged to the appropriate tax account.

C. The net profit from the sale of timber, cord wood, or other property acquired with rights of way or other lands shall be credited to the appropriate land and land rights or clearing land account. Where land is held for a considerable period of time and timber on the land at the time of purchase increases in value, the net profit (after giving effect to the cost of the timber) from the sales of timber or its products shall be credited to account 421, Miscellaneous Nonoperating Income.

D. Separate entries shall be made for the acquisition, transfer, or retirement of each parcel of land, and each land right (except rights of way for distribution lines), or water rights, having a life of more than one year. A record shall be maintained showing the nature of ownership, full legal description, area, map reference, purpose for which used, city, county, and tax district in which situated, from whom purchased or to whom sold, payment given or received, other costs, contract date and number, date of recording of deed, and book and page of record. Entries transferring or retiring land or land rights shall refer to the original entry recording its acquisition.

E. Any difference between the amount received from the sale of land or land rights, less agent's commissions and other costs incident to the sale, and the book cost of such land or land rights, shall be included in account 411.6, Gains from Disposition of Utility Plant, or account 411.7, Losses from Disposition of Utility Plant, Provided such property is recorded in accounts 101-104. If the property

being disposed of is recorded in account 105, Property Held for Future Use, or account 121, Nonutility Property; but had previously been recorded in one of the aforementioned utility plant accounts, gains or losses on its sale shall be credited or charged to account 411.6 or 411.7, as appropriate, otherwise to account 421.1, Gain on Disposition of Property, or account 421.2, Loss on Disposition of Property, unless a reserve therefor has been authorized and provided.

NOTE — Significant gains or losses on sale of property, as determined by the Commission, shall be transferred to account 256, Deferred Gains from Disposition of Property, or account 187, Deferred Losses from Disposition of Property; and amortized to account 411.6, Gains from Disposition of Utility Plant, 411.7, Losses from Disposition of Utility Plant, 421.1, Gain on Disposition of Property or 421.2, Loss on Disposition of Property, as appropriate.

F. The cost of buildings and other improvements (other than public improvements) shall not be included in the land accounts. If at the time of acquisition of any interest in land such interest extends to buildings or other improvements (other than public improvements), which are then devoted to water operations, the land and improvements shall be separately appraised and the cost allocated to land and buildings or improvements on the basis of the appraisals. If the improvements are removed or wrecked without being used in operations, the cost of removing or wrecking shall be charged and the salvage credited to the account in which the cost of the land is recorded.

G. When the purchase of land for utility operations requires the purchase of more land than needed for such purposes, the charge to the specific land account shall be based upon the cost of the land purchased, less the fair market value of that portion of the land which is not to be used in utility operations. The portion of the cost measured by the fair market value of the land not to be used shall be included in account 105, Property Held for Future Use, or account 121, Nonutility Property, as appropriate.

H. Provision shall be made for amortizing amounts

carried in the accounts for limited-term interests in land so as to apportion equitably the cost of each interest over the life thereof. (See account 114, Accumulated Provision for Amortization of Utility Plant in Service, and account 404, Amortization of Limited-Term Utility Plant.)

I. The items of cost to be included in the accounts for land and land rights are as follows:

1. Bulkheads, buried, not requiring maintenance or replacement.
2. Cost, first, of acquisition included mortgages and other liens assumed (but not subsequent interest thereon).
3. Clearing (first cost) the land of brush, trees, and debris.
4. Condemnation proceedings, including court and counsel costs.
5. Consents and abutting damages, payment for.
6. Conveyancers' and notaries' fees.
7. Fees, commissions, and salaries to brokers, agents, and others in connection with the acquisition of the land or land rights.
8. Grading the land, except when directly occasioned by the building of a structure.
9. Leases, cost of voiding upon purchase to secure possession of land.
10. Removing, relocating, or reconstructing property of others, such as buildings, highways, railroads, bridges, cemeteries, churches, telephone and power lines, etc., in order to acquire quiet possession.
11. Retaining walls unless identified with structures.
12. Special assessments levied by public authorities for public improvements on the basis of benefits for new roads, new bridges, new sewers, new curbing, new pavements, and other public improvements, but not taxes levied to provide for the maintenance of such improvements.
13. Surveys in connection with the acquisition, but not amounts paid for topographical surveys and maps

where such costs are attributable to structures or plant equipment erected or to be erected or installed on such land.

14. Taxes assumed, accrued to date of transfer of title.
15. Title, examining, clearing, insuring, and registering in connection with the acquisition and defending against claims relating to the period prior to the acquisition.
16. Appraisals prior to closing title.
17. Cost of dealing with distributees or legatees residing outside of the state or county, such as recording power of attorney, recording will or exemplification of will, recording satisfaction of state tax.
18. Filing satisfaction of mortgage.
19. Documentary stamps.
20. Photographs of property at acquisition.
21. Fees and expenses incurred in the acquisition of water rights, and grants.
22. Cost of fill to extend bulkhead line over land under water, where riparian rights are held, which is not occasioned by the erection of a structure.
23. Sidewalks and curbs constructed by the utility on public property.
24. Labor and expenses in connection with securing rights of way, where performed by company employees and company agents.

* * * *

INCOME ACCOUNTS

1. UTILITY OPERATING INCOME

* * * *

411.6. Gains from Disposition of Utility Plant.

This account shall include amounts relating to gains from the sale or other disposition of utility plant recorded in accounts 101-104; or property recorded in account 105, Property Held for Future Use or account 121, Nonutility Property, which had previously been classified in the aforementioned utility plant accounts. Record income taxes on gains recorded in this account in account 409, Income Taxes.

411.7. Losses from Disposition of Utility Plant.

This account shall include amounts relating to losses from the sale or other disposition of utility plant recorded in accounts 101-104; or property recorded in account 105, Property Held for Future Use or account 121, Nonutility Property, which had previously been classified in the aforementioned utility plant accounts. Record income taxes on gains recorded in this account in account 409, Income Taxes.

* * * *

Supreme Court, U. S.
FILED
FEB 4 1980
MICHAEL RODAK, JR., CLERK

IN THE

Supreme Court of the United States

OCTOBER TERM, 1979

Nos. 79-928
79-936

BRIDGEPORT HYDRAULIC COMPANY
THE LITCHFIELD WATER COMPANY
THE NEW HAVEN WATER COMPANY
CONNECTICUT AMERICAN WATER COMPANY

v.

THE DIVISION OF PUBLIC UTILITY CONTROL
WITHIN THE DEPARTMENT OF BUSINESS REGULATION
OF THE STATE OF CONNECTICUT

ON APPEAL FROM THE SUPERIOR COURT FOR THE JUDICIAL
DISTRICT OF HARTFORD-NEW BRITAIN AT HARTFORD

MOTION TO DISMISS
IN REPLY TO JURISDICTIONAL STATEMENTS

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ON APPEAL FROM THE SUPERIOR COURT FOR THE JUDICIAL
DISTRICT OF HARTFORD-NEW BRITAIN AT HARTFORD

MOTION TO DISMISS
IN REPLY TO JURISDICTIONAL STATEMENTS

Appellee, the Division of Public Utility Control, pursuant to Rule 16 of the Rules of the Supreme Court of the United States, moves that the appellants' appeals from the decision of the Connecticut Superior Court be dismissed on the ground that no substantial federal question has been presented to this Court.

OPINION BELOW

The opinion of the Connecticut Superior Court is not reported. The appellants have attached to their jurisdictional statements copies of the opinion.

JURISDICTION

Three cases were consolidated for trial purposes to the Connecticut Superior Court, a declaratory judgement action taken pursuant to the Connecticut Administrative Procedure Act concerning the validity of certain Connecticut accounting regulations for public service companies and two appeals taken from administrative agency decisions on two public service company rate increase applications. The opinion and order of the Superior Court were entered May 12, 1979. Appellants petitioned the Connecticut Supreme Court for review. Appellants' petition for certification was denied by the Supreme Court on July 24, 1979. A motion for reargument and reconsideration of the appellants' petition for certification was denied by the Supreme Court on September 19, 1979.

The appellants have appealed to this Court and have invoked this Court's jurisdiction under 28 U.S.C. 1257(2).

QUESTION PRESENTED

Whether § 5, 7, 411.6, 411.7, 421.1 and 421.2 of the Connecticut Uniform System of Accounts prescribed for Class A water utilities which provide for the recordation of the gains and losses from utility plant and property dispositions on a utility company's income statement either as part of a company's utility or non-utility operations, rather than in its surplus accounts, are consistent with generally recognized principles of accounting, as those principles apply to the factual realities of Connecticut's utility regulatory environment.

REGULATIONS AND ORDERS

Sections 5, 7, 411.6, 411.7, 421.1 and 421.2 of the Connecticut Uniform System of Accounts prescribed for Class A water utilities are reprinted at p. 2a.

The decisions of the Public Utilities Control Authority in its Docket No. 760701, *Application of the Litchfield Water Company to Increase its Rates to all Customers* and Docket No. 770301, *Application of the Bridgeport Hydraulic Company to Increase its Rates to all Customers* are reprinted at pages 29a and 47a of the Jurisdictional Statement submitted by the Bridgeport Hydraulic Company and The Litchfield Water Company.

STATEMENT OF THE CASE

The appellee is the Division of Public Utility Control of the State of Connecticut,[1] an agency designated by statute to regulate by rule and order the operations and rates of all Connecticut public service companies.

In 1972, the Connecticut Public Utilities Commission duly adopted amendments to the Uniform System of Accounts for Class A water companies[2] and all gas and electric companies. The amendments were adopted to specifically conform the Connecticut Uniform System of Accounts to national changes in the generally recognized principles of accounting promulgated in 1966 by the Accounting Principles Board[3] in its Opinion No. 9, as those principles applied to the realities of Connecticut public utilities' operations. (Appendix, p. 1a) In particular, Connecticut's accounting regulations were amended to require the recordation of gains and losses from the sale, abandonment or other disposition of utility plant, including land and land rights, on a company's income statement, rather than in its surplus accounts. Gains and losses from the disposition of utility plant which had been used and useful in providing utility service to the public were directed "above-the-line"[4] as part of utility operations. Gains and losses from the disposition of a utility company's property which had never been employed in utility service were directed "below-the-line" as part of non-utility operations.

The result of the accounting changes was a more accurate portrayal of the position of utility plant and property dispositions in Connecticut utility company life.

On November 10, 1972, the Connecticut Class A water companies, including the present appellants, requested a declaratory ruling from the Connecticut Court of Common Pleas on the constitutionality of the 1972 accounting amendments. *Greenwich Water Company v. Public Utilities Commission*, Docket No. 108038, Hartford County. The state case was stayed in 1975, however, on the commencement of a declaratory judgement action and a request for injunctive relief brought by the appellant companies to a three judge federal panel. *Bridgeport Hydraulic Company v. Council on Water Company Lands*, 453 F. Supp. 942 (D.Conn. 1977). Included among other issues in the federal case was the companies' contest of the constitutionality of the 1972 amendments to the

---

[1]Formerly the Public Utilities Commission and the Public Utilities Control Authority.

[2]Class A water companies are those water utility companies having annual operating revenues in excess of $50,000.

[3]The Accounting Principles Board is part of the American Institute of Certified Public Accountants. The published opinions of the Board are statements of generally recognized principles of accounting applicable to all businesses, regulated and non-regulated.

[4]Above-the-line accounts represent accounts above the line denoted utility operating income and are associated with a company's utility operations. Below-the-line accounts represent accounts below the line denoted utility operating income and are associated with a company's non-utility operations. In the determination of the reasonableness of a particular utility rate both the return on invested plant (utility operating income) and the return on common equity are considered by the regulatory agency.

Connecticut Uniform System of Accounts. After the presentation of testimony, a stipulation of fact, documentary evidence and argument, the three judge federal panel dismissed the companies' claims against the amendments on alternate grounds: (1) the companies failed to prove that the accounting regulations or their application to the ratemaking process deprived them or their shareholders of any property rights in violation of the Constitution and thus the Court was without power to render an advisory opinion on a hypothetical question and (2) that a possible infringement of a company's constitutional right to a just and reasonable rate in a particular case should properly be addressed to a State Court as the Johnson Act, 28 United States Code 1342, was a bar to federal intervention in state ratemaking. The federal court's decision dismissing the companies' claims against the 1972 accounting regulations was appealed by the companies to this Court, but their appeal was withdrawn.

Subsequent to the federal decision, *Greenwich Water Company v. Public Utilities Commission, supra,* was reactivated in the Connecticut Superior Court. That case was consolidated for trial purposes with two appeals from rate decisions issued by the Public Utilities Control Authority; *Bridgeport Hydraulic Company v. Public Utilities Control Authority*, Docket No. 117874 1, Fairfield County, and *The Litchfield Water Company v. Public Utilities Control Authority*, Docket No. 015775 9, Litchfield County. The two rate decision appeals were presented to the Connecticut Superior Court on the respective administrative records and the declaratory judgement action was presented on a stipulation of fact and an evidentiary record consisting of the testimony and evidence presented to the three judge federal panel in *Bridgeport Hydraulic Company v. Council on Water Company Lands, supra.* (See Appendix p. 6a)

The Connecticut Superior Court dismissed the companies' claims and upheld the validity of the amended accounting regulations. The Court found that the recordation of utility plant

disposition gains and losses either above or below-the-line on the income statement did not constitute a "taking" of the property of the companies or their shareholders, but, instead, was a legislative policy determination consistent with the regulatory circumstances existing in Connecticut. Specifically, the Court held that the companies failed to prove that the amendments were at odds with generally recognized principles of accounting or that the amendments, as they may be applied to particular rate applications, deprive the companies or their shareholders of any constitutionally protected rights.

The companies applied for certification for review to the Connecticut Supreme Court. The Supreme Court denied certification. The companies have now appealed to this Court for review for the 1972 amendments to the Connecticut Uniform System of Accounts. The companies' appeal should be dismissed.

NO SUBSTANTIAL FEDERAL QUESTION EXISTS IN THIS CASE

The companies, in their jurisdictional statements, allege that the issue presented by their appeals to this Court is one of constitutional proportion. The companies claim that the 1972 amendments to the Connecticut Uniform System of Accounts take their property and the property of their shareholders in violation of the Fourteenth Amendment to the United States Constitution. The companies have overstated the case. The existence and operation of the 1972 amendments do not interfere with or impair any of the constitutionally guaranteed rights of either the appellant companies or their shareholders. None of the elements of a taking discussed by this Court in *Penn Central Transportion Company v. New York City*, 438 U.S. 104, exist in this case. The validity of Connecticut's 1972 accounting regulations does not present a question of property right deprivation or a question of ownership to utility property or property disposition proceeds between companies, shareholders or customers. The validity of the 1972 accounting

regulations depends, instead, on a consideration of legislative accounting policy and its relation to the factual reality of Connecticut's regulatory circumstances. *American Telephone & Telegraph Company v. United States*, 299 U.S. 232.

I. The 1972 Amendments to the Connecticut Uniform System of Accounts Do Not Take The Property of the Appellant Companies or Their Shareholders.

Neither the shareholders in an ongoing utility company nor a company's customers have a property interest in the particular assets of a company or in the proceeds from normal asset disposition. The companies' shareholders do not "own" the companies' assets or any appreciation in the value of those assets. *Rhode Island Hospital Trust Co. v. Doughton*, 270 U.S. 69, 81-83; *Silberman v. Blodgett*, 105 Conn. 192, 213. The ownership of stock gives the shareholder the right to share in the management of the corporation, in the profits when declared as dividends and in the assets of the corporation upon dissolution.[5] *DeNuzio v. DeNuzio*, 90 Conn. 342, 345. Stockholders have no interest in the assets of an ongoing utility operation beyond their general interest in the total company. *Eisner v. Macomber*, 252 U.S. 189, 208-209; *Rhode Island Hospital Trust Co. v. Doughton*, 270 U.S. 69. A utility company's ratepayers clearly do not have any legal or equitable interest in a company's assets. *Board of Public Utility Commissioners v. New York Telephone Company*, 271 U.S. 23, 32. A utility company's property and any proceeds from the disposition of its property belong exclusively to the company itself. A utility company's property, however, may be regulated, subject to the protection of certain constitutional guarantees. *Bowles v. Willingham*, 321 U.S. 503, 517-518; *Goldblatt v. Town of Hempstead, New York*, 369 U.S. 590; *Permian Basin Area Rate Cases*, 390 U.S. 747, 769.

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[5]As the Connecticut Uniform System of Accounts only applies to ongoing utility operations and does not operate in utility company dissolutions, shareholders' rights on company dissolution are not affect by the 1972 regulations.

The constitutional guarantees afforded to a utility company and its shareholders are that the end result of utility regulation is a protection of the original amount of capital invested in the enterprise, a reasonable level of revenues to provide a company with continued financial viability and a fair return on the original value of the utility property devoted to public service. *Bluefield Waterworks & Improvements Co. v. Public Service Comm'n.*, 262 U.S. 679, 692-693; *Federal Power Commission v. Hope Natural Gas Co.*, 320 U.S. 591. None of these constitutional guarantees are impaired by the existence or operation of the 1972 amendments to the Connecticut Uniform System of Accounts.

The 1972 amendments do not affect a company's ownership or control of its property. The revised accounting regulations do not require a company to remove any of its utility plant from utility operations and do not require a company to sell any of its property.[6] If and when such property is sold, a company receives the entire amount of the proceeds from the sale, which

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[6]The companies place great stress on the fact that the 1972 regulations may apply to the sale of watershed acreage which the companies have removed from its used and useful status and on which they now receive no return. Contrary to the companies' assertion that State approval is required before property can be *withdrawn* from public service, the record in this case demonstrates that the removal of utility property from its used and useful status is essentially a unilateral act on the part of the companies. State approval is only required prior to the *sale* of such property. Section 16-43 and 16-50c, Connecticut General Statutes. The definitional status of the regulations was necessary to preserve their integrity and avoid a company's sidestepping the 1972 accounts by simply withdrawing property earmarked for profitable disposition from the plant accounts immediately prior to sale and maintaining property involved in loss transactions in the plant accounts during disposition.

All the land that the companies now claim is available for sale was removed from its used and useful status only *after* the adoption of the 1972 amendments. Further, the sale status of such land is not clear because of recent health restrictions placed on the disposition of watershed acreage. Section 25-32, Connecticut General Statutes. Land which the companies have unilaterally determined to be nonessential may, in fact, be necessary for continuing operations, requiring its return to rate base status. The companies' above-described unilateral action should not create an equitable leverage against the amendments.

proceeds remain in its cash reserves until paid out for company purposes by management. No money is paid or given to ratepayers. To the extent that the 1972 accounting regulations require the recordation of the gains or losses from the disposition of property employed in utility service above-the-line and direct gains and losses on the disposition of property not employed in public utility service below-the-line on the income statement, rather than in the surplus accounts, no taking occurs. *Kansas City Southern Ry. Co. v. U.S.*, 231 U.S. 423.

In conformity with constitutional principles, the 1972 accounting regulations protect and guarantee the original investment of the companies and their shareholders in utility plant and property. If a gain is realized on the disposition of utility plant, the original amount invested is returned to the companies free of regulation under the 1972 amendments. If a loss occurs on the disposition or abandonment of utility plant, the original amount invested is protected by the 1972 amendments through an above-the-line recordation of the loss.

To the extent that utility plant disposition gains and losses are considered in the Connecticut ratemaking process,[7] the process provides the companies and their shareholders with a fair return on their investment. This conclusion was reached by

[7]Utility plant disposition proceeds have received varied ratemaking treatment in Connecticut, depending upon the particular rate case and depending upon whether such dispositions have occurred within a company's "test year" (the most recent twelve months of actual financial experience available), the magnitude of the disposition result and whether such dispositions are of a current, recurring nature. The record before this Court contains three rate decisions which did not reflect utility plant disposition proceeds (Exhibits 8, 10 and 12), two decisions in which the proceeds were amortized (Exhibits 14 and 18), and four decisions in which the proceeds were considered on the basis of a yearly average (Exhibits 19 and 20, and PUCA Docket Nos. 780201 and 780303, submitted to the Superior Court at the hearing). Further, in both Docket Nos. 780201 and 780303 proceeds from the disposition of utility property which was not employed in utility service received *below-the-line* accounting and ratemaking treatment, in conformity with the 1972 regulations. Of the nine Connecticut rate decisions involving the appellant companies since the adoption of the accounting amendments, only three have been appealed.

both the Connecticut Superior Court in *Greenwich Water Company v. Public Utilities Commission, supra; Litchfield Water Company v. Public Utilities Control Authority, supra;* and *Bridgeport Hydraulic Company v. Public Utilities Control Authority, supra;* and by the three judge federal panel in *Bridgeport Hydraulic Company v. Council on Water Company Land, supra,* after their review of virtually identical records, including the Connecicut rate decisions which have considered utility plant disposition proceeds.

The Connecticut Superior Court held:

> "There was no showing that the rate of return on investment was inadequate, nor insufficient to attract investors."

The federal Court stated:

> "The present record presents no concrete set of facts which demonstrate that the passage of the 1972 Amendments has caused the shareholders to receive less than such fair return." 453 F. Supp. at p. 953.

Thus, the 1972 amendments do not impair the companies' or their shareholders' constitutional right to a just and reasonable return on their investment. Further, as each rate decision has reflected a revenue level sufficient to meet ongoing revenue requirements, the continued financial viability of the companies has been assured.[8]

[8]The appellant New Haven Water Company has received three Connecticut rate increase decisions which have considered utility property disposition proceeds. (Exhibits 14, 20 and PUCA Docket No. 780201, submitted to the Superior Court) None of these rate decisions were appealed by the company, including PUCA Docket No. 11691 (1975) referred to by the appellant New Haven and Connecticut American Water Companies at p. 7-8 of their Jurisdictional Statement. It must be presumed that the company determined that the rate decisions provided it with just and reasonable revenue levels.

The companies claim, however, that the ratemaking consideration of utility plant disposition proceeds decreases their utility operating expenses and consequently lowers a theoretical level of revenues that they "should" receive. Contrary to the companies' theory, however, the record in this case demonstrates that the companies have at all times received exactly what they have been entitled to; a level of revenues sufficient to provide for continuing operations and for a reasonable return on investment. Proceeds from utility plant dispositions are entirely received and retained by the companies. To the extent that current proceeds are considered in the ratemaking process, the proceeds are available for use in a company's ongoing operations. In a similar manner, to the extent that losses from the disposition or abandonment of utility plant are considered in the ratemaking process, such losses are considered as part of a company's utility operations. There is no difference in effect or constitutional significance between an increase or decrease in a utility company's revenue requirements caused by a gain or loss on the disposition of utility plant and an increase or decrease in revenue requirements caused by any other facet of a company's financial operating experience. Confiscation does not occur when the effect of regulation is the utilization of utility revenues in utility operations.

This Court's decision in *Board of Public Utilities Commissioners v. New York Telephone Co.*, 271 U.S. 23, does not prohibit the regulatory consideration of current utility revenues in current company operations, as occurs under Connecticut's 1972 accounting regulations in conjunction with Connecticut's prospective ratemaking philosophy. *Connecticut Natural Gas Co. v. Public Utilities Comm'n.*, 29 Conn. Sup. 379. *New York Telephone Co.* only prohibits retroactive ratemaking, where past collected revenues are employed to bolster an admittedly unjust and unreasonable future rate level. The issue of retroactive ratemaking and reparations, addressed by this Court in *Board of Public Utilities Commissioners v. New York Telephone Co., supra*, and in *Arizona Grocery Company v. Atchison Topeka and Santa Fe Ry. Co.*, 284 U.S. 370, does not exist in this case. The 1972 amendments only apply to utility plant and property disposition gains and losses which have occurred after 1972 and do not reach back to affect any dispositions or rate decisions that may have occurred prior to their effective date. Past profits are not used to sustain future unreasonable rates. There is no question that Connecticut has provided for all of the companies' revenue requirements and has allowed the companies and their shareholders a just and reasonable return on their investment. Further, the 1972 regulations did not retroactively change the sale or accounting status of any utility company property. At the time of the adoption of the amendments, all of the property which the companies now claim is available for sale was used and useful as utility plant providing utility service to the public. To the extent that the companies' shareholders may have expected utility plant or utility property disposition proceeds to be available elsewhere and not be employed in utility operations, their expectations are not of constitutional significance. The companies' shareholders are shareholders in public service companies. An expectation that utility plant or utility plant disposition gains or losses would not constitute part of utility operations in speculative and does not rise to the level of a constitutionally protected property interest. *Penn Central Transportation Company v. New York City*, 438 U.S. 104, 130. As the adoption of the 1972 accounting amendments had no effect, retroactive or otherwise, on legitimate investor expectations or on shareholders' equitable interests in ongoing utility operations, this Court's decision in *New York Telephone Company* does not constitute a bar to the validity of Connecticut's revised accounting procedure.

The companies have attempted to equate their constitutional right to receive fair market value for any property condemned by the State with their claimed constitutional direction for accounting and ratemaking treatment of utility plant disposition gains and losses. The companies' equation fails. First, the companies' right to just compensation on the condemnation of

their property is undisputed and is not affected by the 1972 amendments. The companies receive and retain the entire amount of any condemnation award.[9] Second, fair market value is not a constitutional standard in utility rate regulation. *Federal Power Commission v. Natural Gas Pipeline Company*, 315 U.S. 575; *Federal Power Commission v. Hope Natural Gas Company*, 320 U.S. 591. A utility company's right to just compensation in the condemnation field translates into the regulatory duty to protect and return the original amount which a company has invested in providing utility service to the public and to provide a company and its shareholders with a reasonable rate of return on the original amount of the investment. *Federal Power Commission v. Hope Natural Gas Company*, 320 U.S. 591, 602-607. Once the above-stated constitutional guarantees are achieved, the exact manner and method employed to attain that result are a matter committed to a regulatory agency's discretion. This principle was stated by this Court as follows:

> "Under the statutory standard of 'just and reasonable' it is the result reached, not the method employed which is controlling.
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> ———
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> The conditions under which more or less might be allowed are not important here. Nor, is it important to determine the various permissible ways in which any rate base on which the return is computed might be arrived at." *Federal Power Commission v. Hope Natural Gas Company*, 320 U.S. 591, 602-603.

As the companies' rights on condemnation of their property are not affected by and do not control Connecticut's regulatory process and as the record in this case clearly demonstrates that the end result of Connecticut's rate regulation is just and

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[9]The appellant New Haven Water Company received in 1978 $1,122,000 from the condemnation of certain of its property. As the property had not been employed in providing utility service to the public, the entire condemnation award, in conformity with the 1972 accounting regulations, received *below-the-line* accounting and ratemaking treatment (PUCA Docket No. 780201).

reasonable, the 1972 amendments to the Connecticut Uniform System of Accounts do not impair any constitutionally protected rights of the companies of their shareholders.

The absence of a constitutional mandate directing a particular accounting or ratemaking treatment for utility property disposition gains and losses is reflected in the diversity of regulatory opinion existing throughout the country. Recordation of utility plant disposition proceeds has been directed to a company's surplus accounts rather than to the income statement in *Boise Water Corp. v. Idaho Public Utilities Commission*, 99 Idaho 158, 578 P.2d 1089 (1978); *City of Lexington v. Lexington Water Co.*, 458 S.W.2d 778 (Ky. 1970) and *Keystone Water Co., White Deer Distric v. Penn. Public Utility Comm'n.*, 19 Pa. Commw. Ct. 292, 339 A.2d 873 (1975). Utility plant disposition proceeds have been approved for consideration in rate regulation proceedings in *Democratic Central Committee v. Washington Metropolitan Transit Service*, 485 F.2d 786; *In Re Revision of Rates Filed by Plainfield-Union Water Co.*, 57 N.J. Super. 158, 154 A.2d 201, 211 (1959); *New York Water Service Corp. v. Public Service Commission*, 12 A.D.2d 122, 208 N.Y.S.2d 857 (1960) and *American Telephone and Telegraph Co.*, 64 FCC 2d 1, 65-66 (1977). The Federal Power Commission provides above-the-line accounting treatment for the disposition of utility property held for future use (Federal Power Commission, Docket No. R-379, Order No. 420, 45 F.P.C. 106, 108) and below-the-line recordation of the proceeds received on the disposition of property employed in public service (Federal Power Commission, Order No. 473, 49 F.P.C. 390). The diverse regulatory decisions regarding utility plant disposition gains and losses do not represent national confusion over constitutional principles requiring resolution by this Court. Instead, the diversity of opinion contained in the above-cited decisions represents the individual regulatory assessment of the regulatory circumstances existing in each particular jurisdiction. The Constitution does not require national uniformity in individual accounting practices or ratemaking policies.

II. The 1972 Amendments to the Connecticut Uniform System of Accounts Are Consistent With Generally Recognized Principles of Accounting and the Factual Realities of Connecticut's Public Utility Operations.

It is clear that the validity of Connecticut's 1972 accounting regulations does not present a question of constitutional proportion which merits consideration by this Court. As with other regulatory accounting provisions, the validity of the 1972 amendments depends upon the assessment of legislative policy and its relationship to fundamental principles of accounting as they apply to the factual circumstances existing in Connecticut. The standard against which Connecticut's 1972 regulations must be tested (and against which the regulations were tested by the Connecticut Superior Court) was established by this Court in *American Telephone & Telegraph Co. v. United States*, 299 U.S. 232. The standard was stated by this Court as follows:

> "This court is not at liberty to substitute its own discretion for that of administrative officers who kept within the bounds of their administrative powers. To show that these have been exceeded in the field of action here involved, it is not enough that the prescribed system of accounts shall appear to be unwise or burdensome or inferior to another. Error or unwisdom is not equivalent to abuse. What has been ordered must appear to be 'so entirely at odds with fundamental principles of correct accounting' (*Kansas City S.R. Co. v. United States*, 231 U.S. 423, 444, 58 L.ed. 296, 305, 34 S.Ct. 125, 52 L.R.A. (N.S.) 1) as to be the expression of a whim rather than an exercise of judgment. *Norfolk & W.R. Co. v. United States*, 287 U.S. 134, 141, 77 L.ed. 218, 222, 53 S.Ct. 52; *Kansas City S.R. Co. v. United States, supra* (231 U.S. 456, 58 L.ed. 309, 34 S.Ct. 125, 52 L.R.A. (N.S.) 1)." *American Telephone & Telegraph Co. v. U.S.* 299 U.S. at pp. 236, 237.

The companies, in their jurisdictional statements, have claimed that the 1972 accounting regulations are unconstitutional on their face and have ignored the existence of the extensive factual record developed in this case (Appendix p. 6a). The 1972 accounting regulations are not unconstitutional on their face. Instead, their validity depends upon and is supported by the facts which exist in the record before this Court. The record demonstrates, in part: utility plant, including utility company land employed in utility service, functions as an integral part of utility company operations (Exhibit 88); the acquisition and disposition of utility plant, including land and land rights, is a normal and ordinary part of Connecticut's water utility business (Exhibit 83) Connecticut has historically allowed losses on utility plant to be recovered, through the ratemaking process, as above-the-line charges (Exhibit 60, Exhibit 79); much of the property which the companies claim will be affected by the 1972 amendments would be available for disposition only after a direct conversion to water filtration systems which would increase the companies' rate bases by $40-60 million and which would also be subject to the amendments on disposition or abandonment (Stipulation, Exhibit 5, 82); the companies' original investment on their property has been protected and maintained and a fair return on that investment has been allowed; and the 1972 amendments are in conformity with the generally recognized principles of accounting promulgated by the Accounting Principles Board and have been sanctioned as a valid alternate accounting procedure by the National Association of Regulatory Utility Commissioners (Exhibits 3, 6, 78 and 79).

In this regard, the nature of the companies' own appeal refutes their contention for a constitutional accounting direction. The companies have conceded the propriety of the 1972 amendments' movement of utility property disposition gains and losses from the surplus accounts to the income statement. (Accounts 421.1 and 421.2) The companies have conceded the validity of the 1972 regulations' above-the-line direction for the gain or loss on the disposition of depreciable items of utility

plant. (Instruction 5, Accounts 411.6 and 411.7) The companies assert to this Court, however, that the Constitution directs a particular accounting treatment for the disposition of non-depreciable items of utility plant, where it does not so direct other items of utility property or operations. The companies' claim is untenable. There is no practical basis for distinguishing depreciable from non-depreciable items of utility plant. All utility plant and all utility plant dispositions constitute an integral and ordinary part of utility operations. (Exhibit 88) Nor is there an economic basis for distinguishing between different items of utility plant. Although depreciation charges are collected annually on depreciable property, non-depreciable property affords a constant rate of return which, over the period of its employment in utility operations, often cumulatively exceeds the original cost by several times (Exhibits 32, 33 and 34). Plainly, there is no economic difference between a gain or loss on the disposition of depreciable as opposed to non-depreciable property. Further, there is no legal basis for distinguishing between the disposition accounting for depreciable and non-depreciable property. Although one Court (*Boise Water Corp. v. Idaho Public Utilities Commission*, 578 P.2d 1089) has held that such a difference exists, the Court based its conclusion on the assertion that ratepayers acquire an equitable *ownership* interest in depreciable property by paying annual depreciation charges. The Court's conclusion, however, is entirely refuted by this Court's dismissal of that theory in *New York Telephone Company, supra*, which the State does not contest and upon which the appellants rely.

The fault with the company's present appeal is that individual portions of the 1972 accounting regulations cannot validly be isolated and taken out of context to support a claim for a particular constitutional accounting mandate for one account, but not for another. The 1972 accounting regulations were amended to conform the accounting treatment of *all* items of gain or loss on the disposition of *all* items of utility plant and property to generally recognized principles of accounting. The

legislative decisions encompassed by Sections 5, 7, 411.6, 411.7, 421.1 and 421.2 are integrated and accurately reflect the nature of utility plant and property and its relation to utility company operations. The legislative decisions contained in those regulations are fully supported by the record in this case.

The Connecticut Superior Court on its review of the record found that the adoption of the 1972 amendments was not arbitrary, illegal or capricious. A review of the Connecticut Superior Court's assessment of the record evidence in this case does not present a substantial federal question.

CONCLUSION

For the reasons stated above, the instant appeals do not present a substantial federal question. This Court's review of the Connecticut Superior Court's decision is not required and the appeals should be dismissed.

Respectfully submitted,

CARL R. AJELLO
Attorney General

By: WILLIAM B. GUNDLING
Assistant Attorney General

with whom on the brief was

PETER J. JENKELUNAS
Assistant Attorney General

APPENDIX

Connecticut Law Journal

July 27, 1971

PUBLIC UTILITIES COMMISSION

Notice

Pursuant to the authority to regulate public service companies vested in it by Title 16 of the General Statutes, the Public Utilities Commission hereby gives notice in accordance with Section 4-42 of the General Statutes of its intent to amend regulations concerning the present Uniform System of Accounts applicable to Electric, Gas and Class "A" Water Companies.

The proposed amendments will modify certain classifications within the existing Uniform System of Accounts.

The following is a summary of the proposed changes:

1. The adoption of the inclusive income statement in harmony with Bulletin 9 of the AICPA (American Institute of Certified Public Accountants). All items of revenues and expenses, including many previously charged or credited directly to surplus, with few exceptions, will be included in the current income statement.

2. The inclusion of the gains or losses on sale of property held for future use and non-utility property in the other income or other income deductions section of the income statement, as appropriate.

3. Include the gains or losses on sale or other disposition of utility plant, in the utility operating income section of the income statement.

4. Transfer the interest charged to construction-credit account from the interest charges section of the income statement

to the other income section in order to negate any unintended implication that entries to this account represent a reduction in interest expenses.

5. Provide for deferrals of income taxes pursuant to the Internal Revenue Service Tax Reform Act of 1969 in those instances where permission to use this method has been obtained from the Commission.

6. For Electric Utilities only. Reclassify nuclear fuels into the utility plant section of the balance sheet, thus distinguishing nuclear fuel from other conventional fuels.

GEORGE J. GRIFFIN.
Executive Secretary

UNIFORM SYSTEM OF ACCOUNTS FOR CLASS A WATER COMPANIES

Instructions

5. Utility Plant Purchased or Sold

F. When utility plant constituting an operating unit or system is sold, conveyed, or transferred to another by sale, merger, consolidation, or otherwise, the book cost of the property sold or transferred to another shall be credited to the appropriate utility plant accounts, including amounts carried in account 117, Utility Plant Acquisition Adjustments. The amounts (estimated if not known) carried with respect thereto in the accounts for accumulated provision for depreciation and amortization and in account 252, Customer Advances for Construction, and account 271, Contributions in Aid of Construction, shall be charged to such accounts and the contra entries made to account 102, Utility Plant Purchased or Sold. Unless otherwise ordered by the Commission, the difference, if any, between (a) the net amount of debits and credits and

(b) the consideration received for the property, less commissions and other expenses of making the sale, shall be included in account 411.6, Gains from Disposition of Utility Plant or account 411.7, Losses from Disposition of Utility Plant, as appropriate. (See account 102, Utility Plant Purchased or Sold.)

7. Land and Land Rights

E. Any difference between the amount received from the sale of land or land rights, less agent's commissions and other costs incident to the sale, and the book cost of such land or land rights, shall be included in account 411.6, Gains from Disposition of Utility Plant, or account 411.7, Losses from Disposition of Utility Plant, provided such property is recorded in accounts 101-104. If the property being disposed of is recorded in account 105, Property Held for Future Use, or account 121, Nonutility Property; but had previously been recorded in one of the aforementioned utility plant accounts, gains or losses on its sale shall be credited or charged to account 411.6 or 411.7, as appropriate, otherwise to account 421.1, Gain on Disposition of Property, or account 421.2, Loss on Disposition of Property, unless a reserve therefor has been authorized and provided.

Accounts

1. UTILITY PLANT

101. Utility Plant in Service Classified.

A. This account shall include the original cost of utility plant, included in the plant accounts prescribed herein and in similar accounts for other utility departments, owned and used by the utility in its utility operations, and having an expectation of life in service of more than one year from date of installation, including such

property owned by the utility but held by nominees. Separate subaccounts shall be maintained hereunder for each utility department.

B. The cost of additions to and betterments of property leased from others, which are includible in this account, shall be recorded in subdivisions separate and distinct from those relating to owned property. (See utility plant instruction 6.)

Income Accounts

1. Utility Operating Income

411.6 Gains from Disposition of Utility Plant.

This account shall include amounts relating to gains from the sale or other disposition of utility plant recorded in accounts 101-104; or property recorded in account 105, Property Held for Future Use or account 121, Nonutility Property, which had previously been classified in the aforementioned utility plant accounts. Record income taxes on gains recorded in this account in account 409, Income Taxes.

411.7 Losses from Disposition of Utility Plant.

This account shall include amounts relating to losses from the sale or other disposition of utility plant recorded in accounts 101-104; or property recorded in account 105, Property Held for Future Use or account 121, Nonutility Property, which had previously been classified in the aforementioned utility plant accounts. Record the reductions in income taxes attributable to losses recorded in this account 409, Income Taxes.

2. Other Income and Deductions

421.1 Gain on Disposition of Property

This account shall be credited with the gain on the

sale, conveyance, exchange or transfer of property other than that property recorded in or previously recorded in, accounts 101-104. (See utility plant instructions 5F, 7E and 10E.) Income Taxes on Gains recorded in this account shall be recorded in account 409, Income Taxes. (See account 411.6. Gains from Disposition of Utility Plant.)

B. Other Income Deductions

421.2 Loss on Disposition of Property.

This account shall be charged with the loss on the sale, conveyance, exchange or transfer of property other than that property recorded in, or previously recorded in, accounts 101-104. (See utility plant instructions 5F, 7E and 10E.) The reduction in income taxes attributable to losses recorded in this account shall be recorded in account 409, Income Taxes. (See account 411.7, Losses from Disposition of Utility Plant.)

No. 10 80 38

GREENWICH WATER COMPANY ET AL — COURT OF COMMON PLEAS

VS. — HARTFORD COUNTY

HOWARD E. HAUSMAN ET AL JUNE 14, 1978

STIPULATION OF FACTS

I. STATEMENT OF FACTS

The parties herein stipulate and agree to the following statement of facts:

Paragraphs 1 to 87 are not printed

II. EXHIBITS

The parties herein stipulate and agree that the following exhibits shall be and are evidence in this case:

(The following exhibits except for Exhibit Nos. 18 and 20 and the Annual Reports for BHC and NHWC for the years 1976 and 1977 were included as part of the record in the federal court in the case captioned *Bridgeport Hydraulic Company* et al vs. *Council on Water Company Lands*, B75-212.)

Exhibit 1 Letter dated January 19, 1972 sent by Public Utilities Commission to all Class A Water Utilities.

Exhibit 2 Notice relating to amendments to Uniform System of Accounts for Class A Water Companies published in July 27, 1971 issues of Connecticut Law Journal.

Exhibit 3 Accounting Principles Board Opinion No. 9 Issued December, 1966.

Exhibit 4 Uniform System of Accounts prescribed for Water Utilities Class A Effective January 1, 1965.

Exhibit 5 Uniform System of Accounts prescribed for Water Utilities Class A as amended Effective January 1, 1972.

Exhibit 6 NARUC (National Associates of Regulatory Utility Commission) Uniform System of Accounts for Class A and Class B Water Companies.

Exhibit 7 United States Federal Power Commission Docket No. R-412, Accounting Treatment to Account for Gains and Losses on the Disposition of Utility Property That Had Been Classified in Utility Service and Consolidated of Certain Depreciation Accounts, dated February 15, 1973.

Exhibit 8 Decision of PUC in Docket No. 11351 (1973) Re: Application of BHC for Amendment to Schedules of Rates.

Exhibit 9 Portions of Testimony and Exhibits in PUC Docket No. 11351 (1973) Re: Applications of BHC for Amendment to Schedules of Rates.

Exhibit 10 Decision of PUC in Docket No. 11550 (1974) Re: Application of NHWC to increase rates.

Exhibit 11 Portions of Testimony and Exhibits in PUC Docket No. 11550 (1974) Re: Application of NHWC to increase rates.

Exhibit 12 Decision of PUC in Docket No. 11639 (1975) Re: Application of BHC to increase rates.

Exhibit 13 Portions of Testimony and Exhibits in PUC Docket No. 11639 (1975) Re: Application of BHC to increase rates.

Exhibit 14 Decision of PUC in Docket No. 11691 (1975) Re: Application of NHWC to increase rates.

Exhibit 15 Portions of Testimony and Exhibits in PUC Docket No. 11691 (1975) Re: Application of NHWC to increase rates.

Exhibit 16 Decision of PUC in Docket No. 11736 (1975) Re: Application of BHC to increase rates.

Exhibit 17 Portions of Testimony and Exhibits in PUC Docket No. 11736 (1975) Re: Application of BHC to increase rates.

Exhibit 18 Decisions of PUCA in Docket No. 760701 (1977) Re: Application of Litchfield Water Company to increase rates.

Exhibit 19 Decision of PUCA in Docket No. 770301 (1977) Re: Application of BHC to increase rates.

Exhibit 20 Decision of PUCA in Docket No. 770323 (1977) Re: Application of NHWC to increase rates.

Exhibit 21 Comparison, Before and After Amendments of Statement of Income.

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Exhibit 25 Example of Effects of Rate Regulation Amendments.

Exhibit 26 Example of Effects of Rate Regulation Amendments 1976-80 Financing Summary (Capital Structure Determined by Coverage).

Exhibit numbering skips from 21 to 25 due to typographical error; no exhibits are omitted.

Exhibit 27 Example of Effects of Rate Regulation Amendment 1976-1980 Financing Summary (Optimum Capital Structure).

Exhibit 28 Illustrations of Raising Funds Through Land Sale Versus Through Stock Issuances.

Exhibit 29 Illustrations of Accounting for Gains on Land Sales.

Exhibit 30 Report of Ward S. Curraw; Rate of Return on Stockholders' Investment in the New Haven Water Company, 1974-1975.

Exhibit 31 Statement of John D. McClellan.

Exhibit 32 Investment Adjusted for Inflation and Opportunity Cost.

Exhibit 33 Investment Adjusted for Inflation and Opportunity Cost.

Exhibit 34 Investment Adjusted for Inflation and Opportunity Cost.

Exhibit 35 Annual Reports BHC '70-'77.

Exhibit 36 A General Review of Landholdings of BHC.

Exhibit 37 Accounting Principles Board Opinion No. 30 Issued June, 1973.

Exhibit 38 Chapter 128 of the Connecticut Public Acts of 1911; Chapter 178 of the Connecticut Public Acts of 1915; Section 5401 of the Connecticut General Statutes, 1949 Revision.

Exhibit 39 Charter of the Bridgeport Hydraulic Company.

Exhibit 40 Charter of the Cornwall Water Company.

Exhibit 41 Charter of the Lakeville Water Company.

Exhibit 41 Charter of the Lakeville Water Company.

Exhibit 42 Charter of the Litchfield Water Company.

Exhibit 43 Charter of the Norfolk Water Company.

Exhibit 44 Charter of the North Canaan Water Company.

Exhibit 45 Charter of the New Haven Water Company.

Exhibit 46 Letter dated July 24, 1974, by Charles W. Horsfall, president of the Litchfield Water Company, addressed to Richard S. Woodhull, chief of the Water Supplies Section, Connecticut Department of Health; letter dated August 20, 1975, by Richard S. Woodhull, chief of the Water Supplies Section, Connecticut Department of Health, addressed to Charles W. Horsfall, president of the Litchfield Water Company.

Exhibit 47 Application of the Litchfield Water Company to the PUC for approval to sell certain real property, dated November 7, 1974.

Exhibit 48 Affidavit of Edwin L. Mitchell, dated April 8, 1976 with the attached PUC document entitled "Bridgeport Hydraulic Co., Rate of Return."

Exhibit 49 Bridgeport Hydraulic Company Exhibit No. 2 entitled "Achieved v. Allowed Rate of Return" submitted to the Public Utilities Commission in PUC Docket No. 11736 (1975).

Exhibit 50 Affidavit of Ronald J. Verrilli, dated June 23, 1975, submitted to the PUC in PUC Docket No. 11736 (1975).

Exhibit 51 Affidavit of Robert W. Reinhert, dated June 23, 1975, submitted to the PUC in PUC Docket No. 11736 (1975).

Exhibit 52 Bridgeport Hydraulic Company Exhibit No. 9 entitled "Projected Capital Budget 1975-1980" submitted to the PUC in PUC Docket No. 11736 (1975).

Exhibit 53 Bridgeport Hydraulic Company Exhibit No. 11, pages 1 and 3, entitled "Comparative Statement of Income 1968 Through Test Year," submitted to the PUC in PUC Docket No. 11351.

Exhibit 54 Bridgeport Hydraulic Company Exhibit No. 10, pages 1 and 5, entitled "Comparative Statement of Income 1970 Through Test Year," submitted to the PUC in PUC Docket No. 11639."

Exhibit 55 Bridgeport Hydraulic Company Exhibit No. 11, pages 1 and 5, entitled "Comparative Statement of Income 1971 Through Test Year," submitted to the PUC in PUC Docket No. 11736.

Exhibit 56 PUC Decision on Application of the Connecticut Light and Power Company to Increase Its Electric and Gas Rates, PUC Docket No. 11552, dated October 7, 1974.

Exhibit 57 Connecticut Light and Power Company Exhibits G15 and G20, submitted to the PUC in PUC Docket No. 11552.

Exhibit 58 PUC Decision on Application of the Hartford Electric Light Company to Increase Its Electric and Gas Rates, PUC Docket No. 11553, dated October 7, 1974.

Exhibit 59 Hartford Electric Light Company Exhibits No. G15 and G20, submitted to the PUC in PUC Docket No. 11553.

Exhibit 60 PUC Decision as Application of the Southern Connecticut Gas Company to Increase Its Rates to All Classes of Customers, PUC Docket No. 11448, dated November 15, 1973.

Exhibit 61 Seventeenth Supplemental Mortgage Indenture of the Bridgeport Hydraulic Company to the City Trust Company, dated September 1, 1960.

Exhibit 62 Excerpts from the Twelfth Supplemental Indenture between the New Haven Water Company and the First New Haven National Bank, dated April 1, 1971.

Exhibit 63 Bridgeport Hydraulic Company 9-⅞% Preferred Stock - Series A, Purchase Agreement, dated December 7, 1970.

Exhibit 64 Bridgeport Hydraulic Company, 11% Preferred Stock - Series B, Purchase Agreement, dated March 26, 1975.

Exhibit 65 Bridgeport Hydraulic Company $7,500,000 First Mortgage 10½% Bonds - Series S, Purchase Agreement, dated March 26, 1975.

Exhibit 66 Indenture Agreement between the Seymour Water Company and The New Haven Bank N.B.A., dated June 1, 1956.

Exhibit 67 Bridgeport Hydraulic Company Maps SH-37, 38, 39, 42, and 43 illustrating the Company's landholdings surrounding the Trap Falls Reservoir and the Company's proposed phases for land disposition.

Exhibit 68 Bridgeport Hydraulic Company Maps EA-20, 21, 27, and 28 illustrating portions of the company's landholdings surrounding the Easton Reservoir and the Company's proposed phases for land disposition.

Exhibit 69 Bridgeport Hydraulic Company Maps EA-14, 15, and 22 illustrating portions of the Company's landholdings surrounding the Saugatuck Reservoir and the Company's proposed phases for land disposition.

Exhibit 70 Bridgeport Hydraulic Company Maps SH-22 and 23 illustrating portions of the Company's proposed Shelton Lakes Project.

Exhibit 71 Bridgeport Hydraulic Company Map SH-18 illustrating the proposed Gray Street Pump Station.

Exhibit 72 New Haven Water Company Maps illustrating the Lake Gaillard System, Sheet No. 7 and Sheet No. 17.

Exhibit 73 New Haven Water Company Maps illustrating the West River System, Sheet Nos. 1, 11, 24, and 26.

Exhibit 74 New Haven Water Company Map illustrating the Wintergreen System, Sheet No. 10.

Exhibit 75 New Haven Water Company Map illustrating the Prospect System, Sheet No. 23.

Exhibit 76 New Haven Water Company's 1974 Annual Report to its stockholders.

Exhibit 77 New Haven Water Company's 1975-1977 Annual Reports to its stockholders.

Exhibit 78 Transcript of Testimony of Edwin L. Mitchell, May 10, 1976.

Exhibit 79 Transcript of Testimony of Edwin L. Mitchell May 11, 1976.

Exhibit 80 Transcript of Testimony of Howard Hausman, May 17, 1976.

Exhibit 81 Transcript of Testimony of Phillip M. Dolan, April 28, 1976.

Exhibit 82 Transcript of Testimony of Ronald J. Verrilli.

Exhibit 83 Transcript of Testimony of William S. Warner, April 27, 1976.

Exhibit 84 Transcript of Testimony of William S. Warner, July 15, 1976.

Exhibit 85 Transcript of Testimony of John M. Kingsland, April 29, 1976.

Exhibit 86 Transcript of Testimony of Jay H. Price, Jr., April 28, 1976.

Exhibit 87 Transcript of Testimony of Jay H. Price, Jr., May 11, 1976.

Exhibit 88 Transcript of Testimony of Richard Woodhull, May 5, 1976.

Exhibit 89 Affidavit of Charles Woods, June 15, 1976.

Supreme Court, U. S.
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IN THE

Supreme Court of the United States

OCTOBER TERM, 1979

Nos. 79-928 — 79-936

BRIDGEPORT HYDRAULIC COMPANY
THE LITCHFIELD WATER COMPANY

v.

THE DIVISION OF PUBLIC UTILITY CONTROL
WITHIN THE DEPARTMENT OF BUSINESS REGULATION
OF THE STATE OF CONNECTICUT, Et Al

THE NEW HAVEN WATER COMPANY
CONNECTICUT AMERICAN WATER COMPANY

v.

THE DIVISION OF PUBLIC UTILITY CONTROL
WITHIN THE DEPARTMENT OF BUSINESS REGULATION
OF THE STATE OF CONNECTICUT, Et Al

ON APPEAL FROM THE SUPERIOR COURT FOR THE JUDICIAL
DISTRICT OF HARTFORD-NEW BRITAIN AT HARTFORD

MOTION TO DISMISS APPELLANTS' JURISDICTIONAL STATEMENTS

BARRY S. ZITSER

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February 12, 1980

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DISTRICT OF HARTFORD-NEW BRITAIN AT HARTFORD

MOTION TO DISMISS APPELLANTS' JURISDICTIONAL STATEMENTS

Pursuant to Rule 16 of the Rules of the Supreme Court of the United States, the appellee, Division of Consumer Counsel ("DCC"), moves that the appellant water companies' appeals from the Decision of the Connecticut Superior Court be dismissed. The ground for dismissal is that there is no substantial federal question presented.

OPINION BELOW

The May 12, 1979 opinion and order of the Connecticut Superior Court, Judicial District of Hartford-New Britain, at Hartford, is unreported. This Decision is reprinted and attached to the appellants' jurisdictional statements.

JURISDICTION

The opinion and order of the Connecticut Superior Court involved three consolidated cases which questioned the validity of certain accounting regulations. The consolidated cases include a declaratory judgment action by the Greenwich Water Company and two administrative appeals by the Bridgeport Hydraulic Company and The Litchfield Water Company from rate decisions.

The appellants petitioned the Connecticut Supreme Court for review of the May 12, 1979 opinion and order of the Connecticut Superior Court. The petition for certification was denied on July 24, 1979. The Connecticut Supreme Court subsequently denied a motion for reargument and reconsideration of the petition for certification on September 19, 1979. The Court also dismissed the joint appeals of the appellant companies on October 2, 1979.

The appellants rely on 28 U.S.C. §1257(2) as the basis for this Court's jurisdiction.

QUESTION PRESENTED

Whether amendments to accounting regulations, applicable to the disposition of utility property by water utilities, constitute a taking of property such that this Court is presented with a substantial federal question.

REGULATIONS AND ORDERS

Sections 7, 411.6 and 411.7 of the Connecticut Uniform System of Accounts prescribed for Class A water companies are reprinted in the appellants' jurisdictional statements.

The rate decisions of the Public Utilities Control Authority in Docket No. 760701, Application of the Litchfield Water Company to Increase Its Rates to All Customers, and Docket No. 770301, Application of the Bridgeport Hydraulic Company to Increase Its Rates To All Customers, are reprinted in the jurisdictional statements of the Bridgeport Hydraulic Company and The Litchfield Water Company.

STATEMENT OF THE CASE

The appellee, Division of Consumer Counsel within the Department of Business Regulation of the State of Connecticut[1], is statutorily authorized pursuant to §16-2a of the Connecticut General Statutes, to advocate the interest of Connecticut consumers with respect to investor-owned utilities. The Division of Consumer Counsel, which was served a copy of the appellants' Jurisdictional Statements, is deemed to be an appellee by Rule 10 of the Rules of the Supreme Court of the United States.

The amendments to the Uniform System of Accounts prescribed for Class A water companies[2] were adopted in 1972 by the Connecticut Public Utilities Commission, the predecessor agency of the Public Utilities Control Authority and the present Division of Public Utility Control. These amendments require that gains and losses from the disposition of utility plant and

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[1]Prior to January 1, 1979, the Division of Consumer Counsel was the Office of Consumer Counsel. Public Act 77-614.

[2]Class A water companies have annual operating revenues in excess of $50,000.

property be included in a company's income statement, as opposed to its earned surplus account. More specifically, the amendments treat the gains or losses from the disposition of utility plant and property which was used for providing utility service as utility operating income.[3] Gains or losses from the disposition of utility plant and property which was never "used and useful", however, are treated differently. The amendments provide that the latter gains or losses be accounted for in non-utility related operating income.

After the adoption of the 1972 accounting regulations, the appellants and other Connecticut Class A water companies challenged the constitutionality of these regulations through a declaratory ruling action in Connecticut Court of Common Pleas. *Greenwich Water Co. v. Public Utilities Commission*, Docket No. 108038, Hartford County. While this case was pending, the appellants sought a declaratory judgment and injunctive relief from a three-judge federal court.

In *Bridgeport Hydraulic Company v. Council on Water Company Lands*, 453 F. Supp. 942 (D. Conn. 1977), the three-judge federal court dismissed the companies' claims, including the constitutional challenge. In addition to finding the Johnson Act, 28 U.S.C. §1342, to be a bar to federal intervention in this area, the court reviewed the constitutional claim. The court held that the companies had not proved that the regulations, on their face or as applied, deprived them of any constitutional property right. The Supreme Court summarily affirmed the dismissal without opinion. 439 U.S. 999 (1978).

After the *Bridgeport* dismissal, the pending state court declaratory ruling in *Greenwich Water Co. v. Public Utilities*

[3]Utility plant and property which is used for providing utility service is included in the company's rate base, on which it earns a return. The term "used and useful" denotes utility plant for this purpose, as opposed to plant which is held for future use.

Commission, supra, was revived. This case was consolidated with two appeals from rate decisions by the Public Utilities Control Authority.[4]

In dismissing the consolidated cases, the Connecticut Superior Court upheld the validity of the 1972 accounting amendments. The Court concluded that there was no constitutional violation, based in part on the fact that "there was no showing that the rate of return on investment was inadequate, nor insufficient to attract investors." The Connecticut Superior Court decision is the highest state court decision from which the appellants seek review.

THE JURISDICTIONAL ALLEGATIONS DO NOT PRESENT A SUBSTANTIAL FEDERAL QUESTION

The appellants claim that the 1972 amendments to the Connecticut Uniform System of Accounts violate the Fourteenth Amendment to the United States Constitution, which prohibits any state from depriving ". . . any person of . . . property without due process of law." In support of this claim, the appellants contend that the amendments result in the taking of company and shareholder property without due process of law, and without just compensation. Despite this claim, the uncontested facts of this case do not raise a substantial federal question. Since there is no "taking" of company or shareholder property, the question of due process or just compensation does not even arise. The adoption of the 1972 amendments to the Connecticut Uniform System of Accounts is essentially a matter of sound regulatory agency discretion.

[4]*Bridgeport Hydraulic Company v. Public Utilities Control Authority*, Docket No.117874 1, Fairfield County, and *The Litchfield Water Company v. Public Utilities Control Authority*, Docket No. 015775 9, Litchfield County.

I

The 1972 Amendments To The Connecticut Uniform System of Accounts Do Not Result In The "Taking" of Property

In order to reach constitutional proportions, the appellants' challenge to the 1972 Amendments to the Connecticut Uniform System of Accounts must show property deprivation, or a "taking" of property. Unless these amendments result in a "taking" of property, there is no constitutional question regarding due process or just compensation. In attempting to elevate their challenge to a constitutional level, the appellants have glossed over this important threshold issue.

The Fourteenth Amendment to the United States Constitution protects a person against state deprivation of property without due process. This Amendment is not a shield against any government action affecting the use or value of private property. Only extremely onerous government regulation amounts to a taking of property. *Goldblatt v. Hempstead*, 369 U.S. 590, 594 (1962). The 1972 accounting amendments, on their face and as applied, do not result in such taking.

In order for state regulation to constitute a "taking" of property, there must be ". . . some diminution in the owner's right of use . . ." *Chacon v. Granata*, 515 F.2d 922, 925 (5th Cir. 1975). The accounting amendments, which the appellants claim violate the Fourteenth Amendment, have no effect on the use of utility property. These amendments, which require a change in accounting, do not mandate any transfer of rights which are incident to ownership. The accounting amendments do not dictate when a utility should dispose of property, or what the terms of disposition should be. There is no interference with the use of utility property. The effect of the amendments is felt only *after* the disposition of utility property.

Even after the disposition of utility property, the appellants are not deprived of any property right. The proceeds from the disposition of utility property are not wrenched away from utility companies into the hands of ratepayers. The accounting changes merely require that gains or losses from the disposition of property used to provide utility service are reflected in utility operating expenses, which are built into rates. The amendments reflect a change in regulatory policy, which is a matter of agency discretion. The appellants have no property right in any particular method of accounting.

The appellants' attempt to translate pre-1972 accounting methods into a constitutionally protected property right must fail. The Fourteenth Amendment provides no greater protection to the appellants than to any other property owner. The fact that a particular accounting method may produce greater profits for a utility does not create a right to such profits. A utility is not entitled to the most profitable accounting treatment, any more than a landowner is entitled to the most profitable use of his property. The due process and just compensation clauses of the Fourteenth Amendment do not insure the most profitable use of any property. *C.F. Lytle Co. v. Clark*, 491 F.2d 834, 838 (10th Cir. 1974).

The appellants have no constitutional right to reap windfall profits. They are only entitled to an opportunity to earn just, reasonable and adequate profits on their original investment. See Section IV, *infra*. The 1972 accounting changes do not infringe on the appellants' constitutional right by taking property to which they are entitled.

II

The 1972 Amendments To The Uniform System Of Accounts Do Not Retroactively Deprive The Appellants Of A Property Right

The appellants, New Haven Water Company and Connecticut American Water Company, allege that the 1972 amend-

ments to the Uniform System of Accounts violate the Fourteenth Amendment prohibition against legislation which retroactively divests property rights. Contrary to the appellants' allegation, the 1972 accounting amendments do not deprive them of any property right. Any diminution in the future potential profits available from the disposition of the appellants' property, which results from the 1972 accounting amendments, is not equivalent to the divestiture of property rights. Since the effect of the accounting amendment is prospective, there is no colorable violation of the Fourteenth Amendment.

The appellants have no vested right in a particular method of accounting for the disposition of utility property. They also have no vested right to receive the highest possible profit from the disposition of utility property. The appellants have attempted to convert an expectation in the accounting treatment of utility property disposition into a vested right. This attempt has no constitutional basis. An expectancy of profits based on no changes in regulation is not a protected property interest. *Usery v. Turner Elkhorn Mining Co.*, 428 U.S. 1, 16 (1975).

Flexibility in prescribing proper accounting treatment is especially necessary in utility regulation. Without such flexibility, regulatory changes to protect the paramount public interests would be virtually impossible. In *Federal Housing Administration v. The Darlington, Inc.*, 358 U.S. 84 (1958), the Supreme Court pointed out the distinction between prospective regulation, which may affect prior rights, and retroactive regulation, which violates the Fourteenth Amendment.

> As stated in *Fleming v. Rhodes*, 331 U.S. 100, 107, "Federal regulation of future action based upon rights previously acquired by the person regulated is not prohibited by the Constitution. *So long as the Constitution authorizes the subsequently enacted legislation, the fact that its provisions limit or interfere with previously acquired rights does not condemn it.* Immunity from federal regulation is not gained through forehanded contracts (emphasis added)."

The appellants have not alleged that there is no authority whatsoever for the adoption of the 1972 amendments. They only challenge the applicability of the amendments to utility land which the companies purchased prior to the amendments. Presumably, the appellants would not challenge the same amendments if they applied only to the disposition of property acquired after the adoption of the amendments. Since there is no question that the Division of Public Utility Control and its predecessor agencies had the authority to adopt regulations requiring specific accounting treatment for the disposition of utility plant, the appellants' challenge to the 1972 amendments is baseless. The fact that the accounting treatment of prospective disposition of utility plant applies to previously purchased property does not invalidate the 1972 amendments. The Supreme Court in *Fleming, supra*, left no doubt over the validity of these challenged amendments.

The appellants' grasping for straws becomes even more apparent by their misplaced reliance on the Contract Clause of the United States Constitution.[3] The appellants claim that the effect of the 1972 amendments is analagous to the issue presented in *Allied Structural Steel Co. v. Spannaus*, 438 U.S. 234 (1978). This claim has no foundation. No contractual relationship exists between the appellants and their shareholders regarding the accounting treatment of future utility plant dispositions.

In *Allied Structural Steel, supra*, the Supreme Court invalidated a Minnesota statute which required private employers who voluntarily provided pension plans to pay a

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[3]The Contract Clause, which is contained in Art. I, §10 of the U.S. Constitution provides:

> "No State shall . . . pass any . . . Law impairing the Obligation of Contracts."

substantial fee if they terminated existing plans or closed an office located in Minnesota. The Court held that the statute violated the Contract Clause of the Constitution by drastically altering the contractual relationship between employers and employees. In effect, ". . . the statute in question here nullifies express terms of the company's contractual obligations and imposes a completely unexpected liablity in potentially disabling amounts." 438 U.S., at 247. The Court in *Allied Structural Steel* never extended the Contract Clause by analogy to non-contractual relationships.

In delineating the scope of the Contract Clause, the Court in *Allied Structural Steel* pointed out that the police power of the States is not obliterated by the Contract Clause. The police power is so extensive that minimal alterations of contractual obligations are tolerable. 438 U.S., at 245. Moreover, the Court noted that:

> "It is the settled law of this court that the interdiction of statutes impairing the obligation of contracts does not prevent the State from exercising such powers as are vested in it for the promotion of the common weal, or are necessary for the general good of the public, though contracts previously entered into between individuals may thereby be affected. This power, which in its various ramifications is known as *the police power, is an exercise of the sovereign right of the Government* to protect the lives, health, morals, comfort and general welfare of the people, *and is paramount to any rights under the contracts between individuals.*" *Mannigault v. Springs*, 199 U.S. 473, 480.

438 U.S., at 241 (emphasis added). Even if the appellants had some contractual right to a particular accounting treatment, the police power inherent in the Division of Public Utility Control and its predecessor agencies must prevail. This overriding

power prompted the Court to note one commentator's view, that:

> "the results might be the same if the contract clause were dropped out of the Constitution, and the challenged statutes all judged as reasonable or unreasonable deprivations of property."[6]

438 U.S., at 241, n.12. In light of the appellants' lack of a contractual or property right in particular accounting treatment, no question regarding the Contract Clause or the Fourteenth Amendment is legitimately raised.

III

There Is No Constitutional Question Regarding the Accounting Treatment Of Utility Plant Disposition

The appellants' attempt to build a substantial federal question out of a strictly state regulatory matter, is contrived. The accounting treatment mandated by the 1972 Amendments to the Uniform System of Accounts is a proper exercise of regulatory authority, which does not raise constitutional issues. The decisions from other jurisdictions regarding the legality of various accounting methods for the gains and losses on the disposition of utility plant reinforce the local nature of accounting procedures.

The appellants correctly state that four courts have held that in particular instances the profit from the sale of a non-depreciable asset that is no longer in service may not be used to reduce rates. *City of Lexington v. Lexington Water Co.*, 458 S.W.2d 778 (Ky. Ct. App. 1970); *Keystone Water Co. v.*

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[6]The appellants misinterpret the commentator to mean "that the Due Process Clause of the Fourteenth Amendment occupies the same Constitutional ground as the Contract Clause."

Pennsylvania Public Utility Commission, 19 Pa. Commw. Ct. 292, 339 A.2d 873 (1975), *aff'd by an equally divided court per curium*, 477 Pa. 594, 385 A.2d 946 (1978); *Boise Water Corp. v. Idaho Public Utilities Commission*, 99 Idaho 158, 578 P.2d 1089 (1978); *Pennichuck Water Works v. New Hampshire*, 103 N.H. 49, 164 A.2d 669(1960). The appellants, however, mistakenly attribute the rationale in *Lexington, supra*, to constitutional considerations. In affirming a trial court decision which reversed a public service commission order, the *Lexington* court relied solely on the commission's uniform system of accounts. Accordingly, the Kentucky accounting system

> provided that a loss upon the sale of land is charged directly to the surplus account — to the shareholders. A profit is credited in the same manner.

458 S.W.2d at 779. The accounting treatment, not constitutional law, was controlling in *Lexington*.

Although constitutional issues were raised in *Keystone, supra*, the case focused on the exclusion of $1.3 million which represented the company's investment in a filtration plant, from the company's rate base for ratemaking purposes. In holding that this investment should have been included in the company's rate base, the court relied on the following principle:

> . . . the rates set by the Commission must not be confiscatory. It has been held that *confiscation results when the order of the Commission refuses the utility company an opportunity to earn a fair return upon the fair value of its property devoted to public service.*

339 A.2d, at 877 (emphasis added). The constitutional issue in *Keystone, supra*, has nothing to do with the accounting treatment of gains or losses resulting from the disposition of utility plant.

The appellants in the instant case have not been deprived of an opportunity to earn a return on property used to provide utility service. Connecticut ratepayers have provided an

adequate return on utility plant formerly included in rate base. The 1972 accounting amendments merely provide that gains or losses on the disposition of utility property be employed in utility operations.

The fact that none of the decisions cited by the appellants raise constitutional issues regarding the accounting treatment of the disposition of utility plant, should dispel any doubt that no substantial federal question is involved. One decision is particularly dispositive on this point. In *Democratic Central Committee v. Washington Metropolitan Area Transit Commission*, 485 F.2d 786 (D.C. Cir. 1973), *cert. denied*, 415 U.S. 935 (1974), the Court of Appeals found no constitutional restrictions in the adoption of regulations dealing with the allocation of land sale gains.

> *We perceive no impediment, constitutional or otherwise, to recognition of a ratemaking principle enabling ratepayers to benefit from appreciations in value of utility properties accruing while in service.* We believe the doctrinal consideration upon which pronouncements to the contrary have primarily rested have lost all present-day vitality.

485 F.2d, at 800 (emphasis added). The court's explicit rejection of constitutional parameters supports the dismissal of the instant appeal for lack of a substantial federal question. The 1972 accounting regulations are not subject to constitutional attack.

IV

The Appellants' Constitutional Rights Are Not Impaired By The 1972 Amendments To The Uniform System of Accounts

The constitutional protections to which the appellants are entitled are of a general nature. The state regulatory process

must protect the original amount of invested capital, and provide a reasonable level of revenues, which enables a utility to pay for operating expenses and earn a fair return on the original value of service related property. *Bluefield Waterworks & Improvements Co. v. Public Service Commission*, 262 U.S. 679, 692-93; *Federal Power Commission v. Hope Natural Gas Co.*, 320 U.S. 591. As long as these protections are afforded, the regulatory agency has broad discretion in carrying out its responsibilities. The 1972 amendments do not encroach upon these constitutional protections.

The appellants' original investment in utility property is not impaired by the 1972 amendments. The accounting of gains or losses from the disposition of utility property does not interfere with setting rates which are "just, reasonable and adequate."[7] The fact that a particular accounting regulation incidentally may benefit ratepayers or shareholders is not constitutionally relevant. As long as the end result of the regulatory process provides a fair balance between shareholder and consumer interests, an accounting regulation is lawful. The appellants are constitutionally entitled to nothing more than a reasonable opportunity to earn the allowed rate of return. *Connecticut Light and Power Co. v. Public Utilities Control Authority*, 40 Conn. L.J. No. 14 at 7. (Supreme Ct. Oct. 3, 1978). The 1972 amendments do not infringe on the regulatory agency's responsibility to set rates which are not confiscatory.

If the appellants' rates do not provide sufficient revenues to produce lawful earnings, they may seek rate relief. Moreover, the appellants may appeal from any decision of the Division of Public Utility Control which does not provide adequate revenues. The appellants' contrived constitutional claim is in effect, a challenge to the sufficiency of all prior rate

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[7]Section 16-19 of the Connecticut General Statutes mandates that rates be just, reasonable and adequate. This is the responsibility of the Division of Public Utility Control, as well as its predecessor agencies, which supercedes all accounting regulations.

decisions. The speciousness of this claim is apparent by the fact that no utility company is challenging the constitutionality of the 1972 accounting treatment for gains on the sale of utility plant, other than land.

Since the appellants exist for the purpose of providing water service to the public, their investment in land was for the same purpose, and not for profit and speculation. The appellants already have been adequately reimbursed for costs incurred in acquiring and holding land. Accordingly, all of their constitutional rights have been protected and guaranteed.

CONCLUSION

For all of the above reasons, the appellants' jurisdictional statements do not present a substantial federal question, and therefore, should be dismissed.

Respectfully submitted,

DIVISION OF CONSUMER COUNSEL

By: BARRY S. ZITSER
Consumer Counsel

with whom on the brief was

VALERIE J. BRYAN
Staff Attorney

Certificate of Compliance with Rule 33

This is to certify that a copy of the foregoing was served on the following, being all counsel of record, by depositing the same in a United States mailbox, first class postage prepaid, to Carl Burns, Esquire, P. O. Box 191, 143 Rowayton Avenue, Rowayton, Connecticut 06853; Harold E. Drew, Esquire, P. O. Box 470, Derby Connecticut 06418; Thomas E. DuPont, Esquire, 23 Academy Street, P. O. Box 267, Danielson, Connecticut 06239; Richard P. Gilardi, Esquire, 855 Main Street, Bridgeport, Connecticut 06604; Robert S. Golden, Jr., Esquire, and William B. Gundling, Esquire, Division of Public Utilities Control, State Office Building, Hartford, Connecticut 06101; Joseloff, August & Sudarsky, 80 State Street, Hartford, Connecticut 06103; Joseloff, August & Sudarsky, 945 Hopmeadow Street, Simsbury, Connecticut 06070; Koskoff & McMahon, 144 West Main Street, Plainville, Connecticut 06062; Maurice Maline, Esquire, 65 Oak View Circle, Bridgeport, Connecticut; Douglas McCallum, Esquire, P. O. Box 176, Unionville, Connecticut 06085; Pinney, Payne, VanLenten & Burrell, 26 West Street, Danbury, Connecticut 06810; Peter A. Treffers, Esquire, P. O. Box 617, New Haven, Connecticut 06509; Rural Water Company, Incorporated, West Redding, Connecticut 06896; Donald F. Keefe, 205 Church Street, New Haven, Connecticut 06114; and to Palmer S. McGee, Jr., Esquire and Allan B. Taylor, Esquire, Day, Berry & Howard, One Constitution Plaza, Hartford, Connecticut 06103 on this 12th day of February, 1980.

BARRY S. ZITSER

Supreme Court, U.S.
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IN THE

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OCTOBER TERM, 1979

NO. 79-928

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THE LITCHFIELD WATER CO.

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Appellee

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MEMORANDUM IN RESPONSE TO MOTIONS TO DISMISS

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ON APPEAL FROM THE SUPERIOR COURT FOR THE JUDICIAL DISTRICT OF HARTFORD-NEW BRITAIN AT HARTFORD

MEMORANDUM IN RESPONSE TO MOTIONS TO DISMISS

The motions to dismiss focus primarily on matters that are not at issue in this appeal. The parties do not dispute the authority of a state to regulate the price charged by a public utility for its services. This regulation is subject only to the constitutional constraint that the state allow the utility a fair opportunity to earn adequate compensation for the devotion of its property to providing public utility service. The constitutional adequacy of the compensation allowed to a utility for the use of its property in

utility service may be gauged according to tests which have been firmly established by this Court's opinions. *See* J.S. 11.[1]

The accounting regulations at issue in this appeal are those which treat the gains on the sale of appellants' property *that has been lawfully withdrawn from utility service*[2] as part of the compensation appellants receive for the utility service provided by that portion of appellants' property that remains devoted to utility service. If appellants and their investors are not the owners of the entire proceeds of the sale of their property that is no longer being used for utility purposes, as the motions to dismiss filed on behalf of the Division of Public Utility Control and the Division of Consumer Counsel assume, appellants concede that regulatory authorities may allocate the gains from such sales as they see fit. On the other hand, if the proceeds of the sale of property that is not dedicated to utility service belong to appellants and their investors, Connecticut's treatment of those proceeds as compensation received by appellants for the service provided by other portions of their property conflicts with the Fourteenth Amendment and with the holding in *Board of Public Utility Commissioners v. New York Telephone Co.*, 271 U.S. 23 (1926). That holding proscribes a regulatory agency from treating a utility's property as if that property were itself part of the compensation that the utility is entitled to have an opportunity to earn in return for the utility service it provides.[3]

[1] "J.S." will be used to refer to the Jurisdictional Statement of appellants Bridgeport Hydraulic Company and The Litchfield Water Company.

[2] The property involved in the appeals by Bridgeport Hydraulic Co. and The Litchfield Water Co. from rate decisions of the Commission was sold by appellants. J.S. 36a, 77a. The accounting regulations at issue apply to the proceeds of property that has been sold. J.S. 94a. Such sales are prohibited unless they receive prior approval from the appropriate regulatory authorities. C.G.S. §§ 16-43, 16-50c.

[3] The principle of *New York Telephone* cannot be restricted, as the motion to dismiss of the Division of Public Utility Control would have it, to a ban on so-called retroactive rate making. If the proceeds from the sale of land that has been lawfully removed from dedication to public service are owned by appellants and their investors, appellants are free to use those proceeds for any lawful purpose. Yet, as the Division of Public Utility Control recognizes, by treating those proceeds as compensation for the provision of utility service, the Connecticut regulatory scheme compels appellants to use the proceeds in their "ongoing operations". Motion to Dismiss at 10. Thus, by treating a utility's property as if it were part of the compensation received by the utility for the public service provided by other portions of that utility's property, Connecticut's accounting regulations effect a compulsory *and uncompensated* dedication of appellants' property to utility service. As *New York Telephone* makes clear, the Fourteenth Amendment does not allow this result.

Thus, the central issue presented by this appeal is whether appellants own all of the proceeds from the sale of land that has been lawfully removed from dedication to public utility service. Decision of this issue was recognized as necessary to its holding both by the superior court below, J.S. 14a-17a, and by the opinion of the United States Court of Appeals for the District of Columbia Circuit on which the superior court relied, *Democratic Central Committee v. Washington Metropolitan Area Transit Commission,* 485 F.2d 786, 800-806 (D.C. Cir. 1973), *cert. denied,* 415 U.S. 935 (1974). Appellants' Jurisdictional Statement has demonstrated that those courts erred when they rejected the "basic legal and economic thesis . . . that utility assets . . . remain exclusively the property of the utility's investors," —a thesis based on "[t]he precept of private ownership historically pervading our jurisprudence . . .," 485 F.2d at 800— in favor of the conclusion that the ownership interest of the utility and its investors in a utility's property, even after that property is no longer used for utility service and has been removed from rate base and sold, is restricted to the amount of the original investment in that property. *Id.* at 801.

The motions to dismiss simply elide this fundamental issue. The appellees are content to argue that if appellants' property has not been physically taken and if appellants are authorized to sell their property, then the fact that the regulations require the gain from the sale to be allocated to rate payers does not constitute a deprivation of property without due process of law. The appellees do not recognize that there is no constitutional difference between (i) a state condemning land without providing just compensation, and (ii) a state, after sale of land by a property owner, depriving the owner of the gain obtained from the sale. The ap-

pellees make no effort to defend the flawed reasoning on which the court below and the District of Columbia Circuit relied, nor do they attempt to provide any other justification for their premise that appellants and their investors do not own the full monetary equivalent of the property which they have sold. Rather, appellees simply assert that there is no constitutional bar to treating the money appellants have received in exchange for their property as if it were compensation received by appellants for the use of other property that remains dedicated to public utility service.

If the motions to dismiss are granted, appellees' assertion will become the law of the land without ever having received plenary review by this Court.[4] Appellants respectfully submit that the question presented is sufficiently important, both as a matter of legal doctrine and because of its practical effect on utilities and regulatory authorities throughout the country, to warrant plenary review.

Respectfully submitted,

Appellants
BRIDGEPORT HYDRAULIC COMPANY
THE LITCHFIELD WATER COMPANY

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[4] The constitutional claims raised here were not presented to the Court in *Bridgeport Hydraulic Co. v. Council on Water Company Lands*, 439 U.S. 999 (1978), *aff'g mem.* 453 F.Supp. 942 (D. Conn. 1972) (3-judge ct.). The district court in that case refused to consider a challenge to the accounting regulations at issue here because of the prohibition on district court action with regard to state utility rates contained in the Johnson Act, 28 U.S.C. § 1342, and because the court believed there to be a ripeness problem in the request for a declaratory judgment. 453 F.Supp. at 952-54.

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